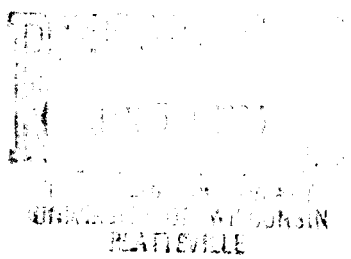
# WORLD POLITICS

*A Quarterly Journal of International Relations*



**Volume 48, Number 2 January 1996**

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

UNDER THE EDITORIAL SPONSORSHIP OF
CENTER OF INTERNATIONAL STUDIES
PRINCETON UNIVERSITY
PUBLISHED BY THE JOHNS HOPKINS UNIVERSITY PRESS

*EDITORIAL BOARD*
John Waterbury, *Chair*
Bruce Bueno de Mesquita, Benjamin J. Cohen, Matthew Evangelista, Judith Goldstein, Stephan Haggard, Peter A. Hall, James R. Hines Jr., Miles Kahler, Jack Levy, James D. Morrow, Elizabeth Perry, Jonas Pontusson, Henry Shue, Vivienne Shue, Jack Snyder, Robert C. Tucker

*Editors:* Nancy Bermeo, Richard D. Challener, George W. Downs, Michael W. Doyle, Richard Falk, Aaron L. Friedberg (*Review Articles*), Robert G. Gilpin, Joanne Gowa, Jeffrey Herbst, Atul Kohli, John Waterbury

*Associate Editors:* Jeremy Adelman, Kent E. Calder, Harold A. Feiveson, Marc A. Levy, John B. Londregan, Kathleen R. McNamara, Pei Minxin, Gilbert Rozman, Anna Seleny, Paul E. Sigmund, Robert L. Tignor, Lynn T. White III, William C. Wohlforth
*Executive Editor:* Ilene P. Cohen; *Assistant Editor:* Susan Bindig
*Secretary:* Patricia D. Zimmer

The editors invite submission of articles (up to 10,000 words, including footnotes) bearing upon problems in international relations and comparative politics. Manuscripts and footnotes should be double-spaced throughout and submitted in triplicate, together with an abstract. Footnotes should be placed at the end of the manuscript. Address: WORLD POLITICS, Bendheim Hall, Princeton University, Princeton, NJ 08544.

Authors may expect to be notified of the editors' decision within four months. Procedures for reviewing manuscripts are based on the anonymity of the author and the confidentiality of readers' and editors' reports. Editorial policy does not provide for transmitting readers' evaluations to authors of rejected manuscripts. Exceptions may be made if, in the opinion of the editors, such comments contain substantive suggestions. WORLD POLITICS does not accept manuscripts that have already been published, are scheduled for publication elsewhere, or have been simultaneously submitted to another journal. Statements of fact and opinion appearing in the journal are made on the responsibility of the authors alone and do not imply the endorsement of the editors or publisher. The journal does not publish communications to the editor or rejoinders to specific articles. Scholars who believe they have been challenged are encouraged to submit an article that will advance the scholarly debate.

*Reprint permission:* Permissions Department, The Johns Hopkins University Press, 2715 N. Charles Street, Baltimore, MD 21218-4319.

*Subscriptions:* WORLD POLITICS, The Johns Hopkins University Press, Journals Publishing Division, 2715 N. Charles Street, Baltimore, MD 21218-4319. Phone: (410) 516-6987; FAX: (410) 516-6968; toll-free (800) 548-1784. Individuals: $25 per year; institutions: $56 per year. Single copies: individuals, $8.00; institutions, $15.00. For postage and handling in Canada and Mexico, add $3.80 per year; outside of North America, $9.00.

*Back Issues:* WORLD POLITICS is available in microfilm or xerographic copies from University Microfilms, Ann Arbor, MI 48106. Two years after publication, complete volumes are available in microfiche form from KTO Microform, Route 100, Millwood, NY 10546. Individual issues in the current and two preceding volumes may be ordered from The Johns Hopkins University Press, Journals Publishing Division, 2715 N. Charles Street, Baltimore, MD 21218-4319.

*Advertising:* Journals Advertising Coordinator, The Johns Hopkins University Press, Journals Publishing Division, 2715 N. Charles Street, Baltimore, MD 21218-4319.

WORLD POLITICS is indexed by *ABC POL SCI, Book Review Index, Combined Retrospective Index Sets (CRIS), Combined Retrospective Index to Book Reviews in Scholarly Journals, 1886–1974 (RSJ), PAIS Bulletin Social Science Index,* and *Periodica Islamica;* it is abstracted and indexed in *United States Political Science Documents, International Bibliography of Periodical Literature (IBZ), International Bibliography of Book Reviews (IBR),* and *Current Military and Political Literature.* Abstracts of articles also appear in *Book Review Digest, Historical Abstracts, International Development Abstracts, International Political Science Abstracts, Political Science Abstracts,* and *Social Sciences Abstracts.*

*Copyright © 1996 by The Johns Hopkins University Press*

WORLD POLITICS (ISSN 0043-8871). Published quarterly by The Johns Hopkins University Press. Vol. 48, No. 2, January 1996. Second class postage paid at Balitmore, MD, and additional mailing offices. POSTMASTER: Send address changes to WORLD POLITICS, The Johns Hopkins University Press, Journals Publishing Division, 2715 N. Charles Street, Baltimore, MD 21218-4319. Printed in the United States of America by Princeton Academic Press.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# WORLD POLITICS

Vol. 48 • January 1996 • No. 2

## CONTENTS

The New Politics of the Welfare State — *Paul Pierson* — 143

Race-Making and the Nation-State — *Anthony W. Marx* — 180

The Breakdown of Hierarchies in the Soviet Union and China: A Neoinstitutional Perspective — *Steven L. Solnick* — 209

Stability and the Distribution of Power — *Robert Powell* — 239

Review Article

Phoenix Risen: The Resurrection of Global Finance — *Benjamin J. Cohen* — 268

The Contributors — ii

Abstracts — iii

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# THE CONTRIBUTORS

PAUL PIERSON is Associate Professor of Government at Harvard University. He is the author of *Dismantling the Welfare State? Reagan, Thatcher and the Politics of Retrenchment* (1994) and coeditor of *European Social Policy: Between Fragmentation and Integration* (1995).

ANTHONY W. MARX is Assistant Professor of Political Science at Columbia University. He is the author of *Lessons of Struggle: South African Internal Opposition, 1960–1990* (1992) and is currently completing a book comparing "race-making" in South Africa, the United States, and Brazil.

STEVEN L. SOLNICK is Assistant Professor of Political Science at Columbia University. He is completing a manuscript on institutional control and collapse in the Soviet Union and is currently conducting research on federal relations in post-Soviet Russia.

ROBERT POWELL is Professor of Political Science at the University of California, Berkeley. His previous work includes *Nuclear Deterrence Theory: The Search for Credibility* (1990). His current work focuses on the effects of political power and the potential use of force on bargaining.

BENJAMIN J. COHEN is Louis G. Lancaster Professor of International Political Economy at the University of California, Santa Barbara. His most recent books include *In Whose Interest? International Banking and American Foreign Policy* (1986) and *Crossing Frontiers: Explorations in International Political Economy* (1991). He is also editor of *The International Political Economy of Monetary Relations* (1993).

Authorization to photocopy items for internal or personal use, or the internal or personal use of specific clients, is granted by The Johns Hopkins University Press for libraries and other users registered with the Copyright Clearance Center (CCC) Transactional Reporting Service, provided that the fee of $3.25 per article is paid directly to CCC, 222 Rosewood Drive, Danvers, MA 01923. 0043-88 71/94 $03.25

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# ABSTRACTS

## The New Politics of the Welfare State

By PAUL PIERSON

This essay seeks to lay the foundation for an understanding of welfare state retrenchment. Previous discussions have generally relied, at least implicitly, on a reflexive application of theories designed to explain welfare state expansion. Such an approach is seriously flawed. Not only is the goal of retrenchment (avoiding blame for cutting existing programs) far different from the goal of expansion (claiming credit for new social benefits), but the welfare state itself vastly alters the terrain on which the politics of social policy is fought out. Only an appreciation of how mature social programs create a new politics can allow us to make sense of the welfare state's remarkable resilience over the past two decades of austerity. Theoretical argument is combined with quantitative and qualitative data from four cases (Britain, the United States, Germany, and Sweden) to demonstrate the shortcomings of conventional wisdom and to highlight the factors that limit or facilitate retrenchment success.

## Race-Making and the Nation-State

By ANTHONY W. MARX

Why was official racial domination enforced in South Africa and the United States, while nothing comparable to apartheid or Jim Crow was constructed in Brazil? Slavery and colonialism established the pattern of early discrimination in all three cases, and yet the postabolition racial orders diverged. Miscegenation influenced later outcomes, as did economic competition, but neither was decisive. Interpretations of these historical and economic factors were shaped by later developments. This article argues that postabolition racial orders were significantly shaped by the processes of nation-state building in each context. In South Africa and the United States ethnic or regional "intrawhite" conflict impeding nation-state consolidation was contained by racial domination. Whites were unified by excluding blacks, in an ongoing dynamic that took different forms. Continued competition and tensions between the American North and South or South Africa's English and Afrikaners were repeatedly resolved or diminished through further entrenchment of Jim Crow or apartheid. With no comparable conflict requiring reconciliation in Brazil, no official racial domination was constructed, although discrimination continued. The dynamics of nation-state building are then reviewed to explain variations in black mobilization and the end of apartheid and Jim Crow.

## The Breakdown of Hierarchies in the Soviet Union and China

### A Neoinstitutional Perspective

By STEVEN L. SOLNICK

Why did modest attempts to decentralize the centrally administered Soviet system lead to its collapse, while more far-reaching decentralization in China left central political and administrative hierarchies intact? This article analyzes the disintegration of centrally planned organizations in the context of a neoinstitutional model of the breakdown of authority within hierarchies. An agency model of hierarchy is presented that incorporates the ambiguous property rights, authority relations, and risk-sharing conditions that prevailed under central planning and then persist during postcommunist transitions. This model suggests that decentralizing reforms could trigger an organizational "bank run," prompting local agents to seize organizational assets under their control. The article also considers reputation-preserving strategies that central authorities might use to avert disintegration.

As an application of this model, the collapse of Soviet political, industrial, and state fiscal hierarchies are considered and compared with the experience of analogous sectors in China. Reforms in both states transferred significant autonomy from the center to local field agents. In the Soviet case these agents appropriated organizational assets with little interference from the center. In China, by contrast, the center preserved both its capacity for monitoring and its reputation for disciplining transgressions; and the rise of hybrid ownership forms made expropriation of state and Party assets far less attractive.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

STABILITY AND THE DISTRIBUTION OF POWER
By ROBERT POWELL

The relation between stability and the distribution of power is an important and long-debated problem in international relations theory. The balance-of-power school argues that an even distribution of power is more stable, while the preponderance-of-power school argues that a preponderance of power is more stable. Empirical efforts to estimate this relation have yielded contradictory results. This essay examines the relation between stability and the distribution of power in an infinite-horizon game-theoretic model in which two states are bargaining about revising the international status quo. The states make offers and counteroffers until they reach a mutually acceptable settlement or until one of them becomes so pessimistic about the prospects of reaching an agreement that it uses force to impose a new settlement. The equilibrium of the game contradicts the expectations of both schools and offers an explanation for the conflicting empirical estimates. In the model stability is greatest when the status quo distribution of benefits reflects the expected distribution of benefits that the use of force would impose.

PHOENIX RISEN: THE RESURRECTION OF GLOBAL FINANCE
By BENJAMIN J. COHEN

Of all the many changes of the world economy since World War II, few have been nearly so dramatic as the resurrection of global finance. A review of five recent books suggests considerable diversity of opinion concerning both the causes and the consequences of financial globalization, leaving much room for further research. Competing historical interpretations, stressing the contrasting roles of market forces and government policies, need to be reexamined for dynamic linkages among the variables they identify. Likewise, impacts on state policy at both the macro and micro levels should be explored more systematically to understand not just whether constraints may be imposed on governments but also how and under what conditions, and what policymakers can do about them. Finally, questions are also raised about implications for the underlying paradigm conventionally used for the study of international political economy and international relations more generally.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# THE NEW POLITICS OF THE WELFARE STATE

By PAUL PIERSON*

THE much-discussed crisis of the welfare state is now two decades old. The tremendous twentieth-century expansion of social programs has been a remarkable feature of advanced industrial societies. In all these countries the welfare state is a core institution, accounting for between one-fifth and one-third of GNP. Ever since the postwar economic boom ended in the early 1970s, however, social programs have faced mounting political challenges. Questions of expansion have long since given way to an acknowledgment of the limits to welfare state growth and the prospect for extended austerity. Despite this fundamental change, however, we still know stunningly little about the politics of social policy retrenchment. In contrast to our vast knowledge of the dynamics of welfare state expansion—arguably the most well-tilled subfield of comparative public policy—welfare state retrenchment remains largely uncharted terrain.[1] Theoretically informed discussion has been limited to very abstract commentaries or the rather reflexive, often implicit application of propositions derived from the study of social policy expansion.

This puzzling state of affairs results in part from the very success of earlier scholarship. The quality of historical research on the welfare state has encouraged a simple process of borrowing already developed models for the examination of a new environment. I would argue, however, that there are compelling reasons to reject such a straightforward extrapolation, that the new politics of the welfare state is instead quite different from the old. Welfare state expansion involved the enactment of *popular* policies in a relatively undeveloped interest-group environment. By contrast, welfare state retrenchment generally requires elected

* I am grateful to the Russell Sage Foundation for financial and administrative support and to Miguel Glatzer for considerable research assistance, as well as helpful comments.

[1] On welfare state expansion, see Gösta Esping-Andersen, *The Three Worlds of Welfare Capitalism* (Princeton: Princeton University Press, 1990); and Evelyne Huber, Charles Ragin, and John D. Stephens, "Social Democracy, Christian Democracy, Constitutional Structure, and the Welfare State," *American Journal of Sociology* 99 (November 1993).

*World Politics* 48 (January 1996), 143–79

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

officials to pursue *unpopular* policies that must withstand the scrutiny of both voters and well-entrenched networks of interest groups. It is therefore not surprising that variables crucial to understanding the former process are of limited use for analyzing the latter one.

This essay seeks to lay the foundations for an analysis of welfare state retrenchment. I emphasize the critical constraints on reform resulting from the role of supportive interest groups and, ultimately, voters.[2] The growth of the welfare state itself transforms the politics of social policy. As a result, the welfare state has proved to be far more resilient than other key components of national political economies and far more durable than existing theories of the welfare state would lead one to expect. The argument is presented in four stages. Section I highlights the characteristic qualities of retrenchment politics. Section II discusses in more detail the principal theories of welfare state expansion and suggests why the distinctiveness of retrenchment makes a straightforward application of these arguments to the contemporary welfare state problematic. Section III explores the dynamics of retrenchment in four cases: Great Britain, the United States, Germany, and Sweden. Section IV builds on this theoretical and empirical analysis to offer some basic propositions about retrenchment politics.

## I. Why the Politics of Retrenchment Is Different

This essay's central claim is that because retrenchment is a distinctive process, it is unlikely to follow the same rules of development that operated during the long phase of welfare state expansion. There are two fundamental reasons for this. First, the political *goals* of policymakers are different; second, there have been dramatic changes in the political *context*. Each of these points requires elaboration.

There is a profound difference between extending benefits to large numbers of people and taking benefits away.[3] For the past half century, expanding social benefits was generally a process of political credit claiming. Reformers needed only to overcome diffuse concern about tax rates (often sidestepped through resort to social insurance "contributions") and the frequently important pressures of entrenched interests. Not surprisingly, the expansion of social programs had until recently

[2] In this sense, my analysis parallels Verdier's recent effort to interpret foreign trade policy as "the outcome of a process influenced by voters." Daniel Verdier, *Democracy and International Trade: Britain, France and the United States, 1860–1990* (Princeton: Princeton University Press, 1994), xv.

[3] R. Kent Weaver, "The Politics of Blame Avoidance," *Journal of Public Policy* 6 (October–December 1986).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

been a favored political activity, contributing greatly to both state-building projects and the popularity of reform-minded politicians.[4]

A combination of economic changes, political shifts to the right, and rising costs associated with maturing welfare states has provoked growing calls for retrenchment. At the heart of efforts to turn these demands into policy have been newly ascendant conservative politicians. Conservative governments have generally advocated major social policy reforms, often receiving significant external support in their effort, especially from the business community.[5] Yet the new policy agenda stands in sharp contrast to the credit-claiming initiatives pursued during the long period of welfare state expansion. The politics of retrenchment is typically treacherous, because it imposes tangible losses on concentrated groups of voters in return for diffuse and uncertain gains. Retrenchment entails a delicate effort either to transform programmatic change into an electorally attractive proposition or, at the least, to minimize the political costs involved. Advocates of retrenchment must persuade wavering supporters that the price of reform is manageable—a task that a substantial public outcry makes almost impossible.

Retrenchment is generally an exercise in blame avoidance rather than credit claiming, primarily because the costs of retrenchment are concentrated (and often immediate), while the benefits are not. That concentrated interests will be in a stronger political position than diffuse ones is a standard proposition in political science.[6] As interests become more concentrated, the prospect that individuals will find it worth their while to engage in collective action improves. Furthermore, concentrated interests are more likely to be linked to organizational networks that keep them informed about how policies affect their interests. These informational networks also facilitate political action.

An additional reason that politicians rarely get credit for program cutbacks concerns the well-documented asymmetry in the way that voters react to losses and gains. Extensive experiments in social psy-

[4] Peter Flora and Arnold J. Heidenheimer, eds., *The Development of Welfare States in Europe and America* (New Brunswick, N.J.: Transaction, 1982).

[5] As recent research has suggested, it would be wrong to treat business as always and everywhere opposed to welfare state programs. For illuminating studies of the United States, see, for example, Colin Gordon, *New Deals: Business, Labor, and Politics in America, 1920–1935* (Cambridge: Cambridge University Press, 1994); and Cathie Jo Martin, "Nature or Nurture? Sources of Firm Preference for National Health Reform," *American Political Science Review* 89 (December 1995). Nonetheless, it is clear that *most* business organizations in all the advanced industrial democracies have favored—often vehemently—cutbacks in the welfare state over the past fifteen years.

[6] Mancur Olson, *The Logic of Collective Action: Public Goods and the Theory of Groups* (Cambridge: Harvard University Press, 1965); James Q. Wilson, *Political Organizations* (New York: Basic Books, 1973), 330–37.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

chology have demonstrated that individuals respond differently to positive and negative risks. Individuals exhibit a *negativity bias*: they will take more chances—seeking conflict and accepting the possibility of even greater losses—to prevent any worsening of their current position.[7] Studies of electoral behavior, at least in the United States, confirm these findings. Negative attitudes toward candidates are more strongly linked with a range of behaviors (for example, turnout, deserting the voter's normal party choice) than are positive attitudes.[8]

While the reasons for this negativity bias are unclear, the constraints that it imposes on elected officials are not. When added to the imbalance between concentrated and diffuse interests, the message for advocates of retrenchment is straightforward. A simple "redistributive" transfer of resources from program beneficiaries to taxpayers, engineered through cuts in social programs, is generally a losing proposition. The concentrated beneficiary groups are more likely to be cognizant of the change, are easier to mobilize, and because they are experiencing losses rather than gains are more likely to incorporate the change in their voting calculations. Retrenchment advocates thus confront a clash between their policy preferences and their electoral ambitions.

If the shift in goals from expansion to cutbacks creates new political dynamics, so does the emergence of a new *context*: the development of the welfare state itself. Large public social programs are now a central part of the political landscape. As Peter Flora has noted, "Including the recipients of [pensions,] unemployment benefits and social assistance—and the persons employed in education, health and the social services—in many countries today almost 1/2 of the electorate receive transfer or work income from the welfare state."[9] With these massive programs have come dense interest-group networks and strong popular attachments to particular policies, which present considerable obstacles to reform. To take one prominent example, by the late 1980s the American Association of Retired People (AARP) had a membership of twenty-eight million and a staff of thirteen hundred (including a legislative

[7] Daniel Kahneman and Amos Tversky, "Prospect Theory: An Analysis of Decision under Risk," *Econometrica* 47 (March 1979); idem, "Choices, Values and Frames," *American Psychologist* 39 (April 1984).

[8] Howard S. Bloom and H. Douglas Price, "Voter Response to Short-Run Economic Conditions: The Asymmetric Effect of Prosperity and Recession," *American Political Science Review* 69 (December 1975); Samuel Kernell, "Presidential Popularity and Negative Voting: An Alternative Explanation of the Midterm Congressional Decline of the President's Party," *American Political Science Review* 71 (March 1977); and Richard R. Lau, "Explanations for Negativity Effects in Political Behavior," *American Journal of Political Science* 29 (February 1985).

[9] Peter Flora, "From Industrial to Postindustrial Welfare State?" *Annals of the Institute of Social Science*, special issue (Institute of Social Science, University of Tokyo) (1989), 154.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

staff of more than one hundred).[10] The maturation of the welfare state fundamentally transforms the nature of interest-group politics. In short, the emergence of powerful groups surrounding social programs may make the welfare state less dependent on the political parties, social movements, and labor organizations that expanded social programs in the first place. Nor is the context altered simply because welfare states create their own constituencies. The structures of social programs may also have implications for the decision rules governing policy change (for example, whether national officials need the acquiescence of local ones) and for how visible cutbacks will be. "Policy feedback" from earlier rounds of welfare state development is likely to be a prominent feature of retrenchment politics.[11]

In short, the shift in goals and context creates a new politics. This new politics, marked by pressures to avoid blame for unpopular policies, dictates new political strategies.[12] Retrenchment advocates will try to play off one group of beneficiaries against another and develop reforms that compensate politically crucial groups for lost benefits. Those favoring cutbacks will attempt to lower the visibility of reforms, either by making the effects of policies more difficult to detect or by making it hard for voters to trace responsibility for these effects back to particular policymakers.[13] Wherever possible, policymakers will seek broad consensus on reform in order to spread the blame. Whether these efforts succeed may depend very much on the structure of policies already in place. As I argue in the next section, theoretical discussions of the welfare state have failed to take this point sufficiently to heart.

## II. The Limits of Existing Theories

Each of the main theories of welfare state expansion—arguments about economic development, arguments about the power of the left, and arguments about institutions—has been loosely appropriated for discussions of the contemporary welfare state. In this section I make explicit the kinds of claims that an inversion of existing theories of expansion might suggest for a theory of retrenchment. While each perspective

[10] Christine L. Day, *What Older Americans Think: Interest Groups and Aging Policy* (Princeton: Princeton University Press, 1990), 25–26.

[11] Gösta Esping-Andersen, *Politics against Markets: The Social Democratic Road to Power* (Princeton: Princeton University Press, 1985); Paul Pierson, "When Effect Becomes Cause: Policy Feedback and Political Change," *World Politics* 45 (July 1993).

[12] Weaver (fn. 3); Paul Pierson, *Dismantling the Welfare State? Reagan, Thatcher and the Politics of Retrenchment* (Cambridge: Cambridge University Press, 1994), chap. 1.

[13] R. Douglas Arnold, *The Logic of Congressional Action* (New Haven: Yale University Press, 1990).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

contains insights, my main contention is that a convincing analysis of retrenchment must move beyond these formulations.

## A New "Logic of Industrialism"?

The earliest well-developed theory of welfare state growth, associated particularly with the work of Harold Wilensky, stressed the relationship of welfare state expansion to processes of economic growth.[14] Welfare state effort was correlated with affluence, suggesting that "strong economies produce strong welfare states." Yet while this argument explained broad social policy differences between rich and poor nations, it proved to be far less helpful in explaining differences *within* the club of rich democracies.

Nonetheless, versions of economic determinism have been prominent in discussions of the contemporary welfare state. The claim that a new "logic of industrialism" encourages a convergence of national social policy models is based on asserted consequences of global economic change.[15] One possibility is that the globalization of capital markets removes crucial economic policy tools from national governments and constrains social policy options. However, as Garrett and Lange have persuasively argued, while monetary and fiscal policies may face new restrictions, there is little evidence that supply-side policies of transfers and services need be constrained, so long as tax bases remain sufficient to insure relatively low deficits.[16] Some social policies may in fact contribute to economic growth, for example, by encouraging the formation of human capital and certain kinds of labor market flexibility.

A related argument is that heightened economic integration will result in what Europeans call "social dumping." The term refers to the possibility that firms operating where "social wages" are low may be able to undercut the prices of competitors, forcing higher-cost firms either to go out of business, or to relocate to low social wage areas, or to pressure their governments to reduce social wage costs. In extreme scenarios these actions could fuel a downward spiral in social provision, eventually producing very rudimentary, lowest-common-denominator national welfare states.[17] The evidence for a process of social dumping

[14] Wilensky, *The Welfare State and Equality* (Berkeley: University of California Press, 1975).

[15] One could fill a small library with books and articles that make this claim. For a good recent example, see Herman Schwartz, "Small States in Big Trouble: State Reorganization in Australia, Denmark, New Zealand, and Sweden in the 1980s," *World Politics* 46 (July 1994).

[16] Geoff Garrett and Peter Lange, "Political Responses to Interdependence: What's Left for the Left," *International Organization* 45 (1991).

[17] For a classic treatment of this dynamic, see William L. Cary, "Federalism and Corporate Law: Reflections on Delaware," *Yale Law Journal* 83 (March 1974).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

remains limited. The social wage is only one factor in investment decisions, and firms will not invest in countries with low social wages unless other factors (for example, infrastructure, worker productivity) justify such investments.[18] Neoclassical trade theory suggests that countries with high social wages should not face problems so long as overall conditions allow profitable investment.[19]

A further, critical objection to the economic determinist argument has received less attention. Even if a high social wage were associated with poor economic performance, the assumption that downward adjustments in social policy would necessarily follow is unjustified. As North has recently reminded us, countries have maintained widely different levels of economic performance for very long periods of time, without marked pressures toward convergence.[20] In a world where particular arrangements have been institutionalized and where local actors have adopted strategies that succeed in local terms, there is no automatic or necessary movement toward any particular definition of efficiency—market dictated or otherwise. Politicians in democratic systems generally worry first and foremost about getting elected. Helping improve the economy may make that easier, but not if it requires hugely unpopular policies, and not if the economic benefits are likely to appear at some point in the distant (that is, postelection) future.

Thus, even if social dumping arguments proved valid—a big if—much would still depend on the balance of political forces favoring and resisting a substantial restructuring of the welfare state. Tendencies toward fragility must be weighed against the considerable sources of wel-

[18] Peter Lange, "The Politics of the Social Dimension," in Alberta Sbragia, ed., *Euro-politics* (Washington, D.C.: Brookings Institution, 1992). For evidence casting doubt on the proposition that systems of social protection have significant negative effects on economic performance, see Rebecca M. Blank, ed., *Social Protection versus Economic Flexibility: Is There a Trade-off?* (Chicago: University of Chicago Press, 1994).

[19] "Unraveling" could occur in a more subtle way, as heightened capital mobility strengthens the bargaining position of business, leading to the gradual erosion of "tightly coupled" systems of industrial relations and, perhaps, welfare states. For a good example of this kind of argument, see Wolfgang Streeck, "From Market-Making to State-Building? Reflections on the Political Economy of European Social Policy," in Stephan Leibfried and Paul Pierson, eds., *European Social Policy: Between Fragmentation and Integration* (Washington, D.C.: Brookings Institution, 1995). While such a scenario cannot be ruled out, the evidence for it remains quite limited. These arguments appear to be more popular among those, like Streeck, who focus on industrial relations systems. See, for example, Jonas Pontusson and Peter Swenson, "Labor Markets, Production Strategies, and Wage Bargaining Institutions: The Swedish Employer Offensive in Comparative Perspective," *Comparative Political Studies* (forthcoming); and Kathleen Thelen, "West European Labor in Transition: Sweden and Germany Compared," *World Politics* 46 (October 1993). Industrial relations systems, however, seem more fragile than welfare state structures. Welfare states, I will suggest, have considerably broader bases of support, which promote the restoration of equilibrium and inhibit the kind of unraveling that occurs in some industrial relations systems.

[20] Douglass C. North, *Institutions, Institutional Change, and Economic Performance* (Cambridge: Cambridge University Press, 1990).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

fare state stability. In short, policy outcomes cannot be derived directly from economic trends. The new logic of industrialism suffers from many of the defects of the old one. Expansive claims of economic determinism pay insufficient attention to the *politics* of policy change. The same cannot be said about power resource and institutionalist arguments, to which I now turn.

## Left Power Resources and the Politics of Retrenchment

The power resources perspective, which attributes cross-national variations in social provision largely to differences in the distribution of political resources among classes, has been the leading approach in comparative politics to explaining patterns of welfare state expansion.[21] Class-based struggle over social provision occurs because social programs affect the bargaining position of workers and employers. Many social programs limit the economic vulnerability of wage earners and increase worker solidarity. According to power resource theorists, strong unions and left parties contribute to the growth of these programs. The power resources approach has had considerable success in accounting for cross-national variations in social provision during the three decades following World War II. Furthermore, the replacement of crude social expenditure data with more fine-grained distinctions among patterns of social provision has greatly improved the model's explanatory power.[22]

A straightforward application of power resource arguments to retrenchment would suggest that welfare states are in deep trouble. The power of organized labor and left parties has shrunk considerably in many advanced industrial societies. As I will argue in Section III, however, there is very little evidence that this decline has had a fundamental impact on welfare states. Cutbacks in social programs have been far more moderate than the sharp drop in labor strength in many countries might lead one to expect, and there appears to be little correlation between declines in left power resources and the magnitude of retrenchment.

The shift in both context and goals that characterizes the new politics of the welfare state helps to explain why this is so. Analysis of the contemporary welfare state's supporters must include not only orga-

[21] John D. Stephens, *The Transition from Capitalism to Socialism* (London: Macmillan, 1979); Walter Korpi, *The Democratic Class Struggle* (London: Routledge, 1983); Esping-Andersen (fn. 11); Walter Korpi, "Power, Politics, and State Autonomy in the Development of Social Citizenship: Social Rights during Sickness in Eighteen OECD Countries since 1930," *American Sociological Review* 54 (June 1989).

[22] Esping-Andersen (fn. 1); Huber, Ragin, and Stephens (fn. 1).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

nized labor and left parties but also the more varied constituencies of individual programs. Interest groups linked to particular social policies are now prominent political actors. The rise of these interest groups is one of the clearest examples of how policy feedback from previous political choices can influence contemporary political struggles. Groups of program beneficiaries did not build the welfare state, but the welfare state contributed mightily to the development of these groups. By the time a politics of austerity began to emerge in the mid-1970s, most welfare state programs were connected to extensive networks of social support. Most prominent were the recipients of the various benefits—pensioners, the disabled, health care consumers. The providers of public services also had a major stake in sustaining expenditure and were usually well organized.[23] Finally, there was a range of public-interest organizations seeking to protect those too weak to mobilize on their own. Indeed, even when groups of recipients are not particularly well organized, politicians may have reason to be attentive to their concerns. Cutbacks, if recognized, are likely to incense voters, and political competitors stand ready to exploit such opportunities. The possibility of exacting punishment at the polls means that the *potentially mobilized* influence policymakers even in the absence of ongoing organized activity.[24]

Thus, there are good reasons to believe that the centrality of left party and union confederation strength to welfare state outcomes has declined. The diminished relevance of power resource arguments reflects the fact that welfare states are now mature and that retrenchment is not simply the mirror image of welfare state expansion. In a context where public social provision is just emerging, the existence of very broad organizations pushing an expansionist policy agenda may be crucial. However, the unpopularity of program cutbacks and the emergence of new bases of support will give politicians pause even where unions and left parties are weak. Equally important, maturing social programs develop new bases of organized support that have substantial autonomy from the labor movement. This shifting base of support may have consequences for the dynamics of policy development, but the weakening of organized labor need not translate automatically into a commensurate weakening of the welfare state.

[23] In this respect, organized labor (public employee unions) continues to be of significance, although not in the way posited by power resource theorists. Union interests are now linked primarily to the employment-generating effects of specific public programs rather than to the broad consequences of generous public provision for the bargaining position of workers.

[24] On this point, see Arnold (fn. 13).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## New Institutionalism and Welfare State Politics

Patterns of governance matter. The "new institutionalist" resurgence in political science reflects a renewed appreciation of how relatively stable, routinized arrangements structure political behavior.[25] The political institutions of different countries vary along crucial dimensions, such as the rules of electoral competition, the relationship between legislature and executive, the role of the courts, and the place of subnational governments in politics. Institutions establish the rules of the game for political struggles—influencing group identities, policy preferences, and coalitional choices, and enhancing the bargaining power of some groups while devaluing that of others. Institutions also affect government capacities—their administrative and financial resources for fashioning policy interventions.

In the field of comparative social policy, the claim that political institutions must be considered consequential structures has been developed primarily in the work of Theda Skocpol and her collaborators.[26] These researchers have raised significant questions about the dynamics of welfare state development, pointing out, for example, that the power resources approach has had little success in accounting for pre–World War II social policy developments. The new institutionalist research agenda, however, has centered on explaining "American exceptionalism"—the belated and halfhearted development of social welfare policies in the United States. Just as a focus on Sweden was central to the development of the power resources model, concentration on the United States has underscored the importance of political institutions.

Institutionalists make two broad claims about welfare state development. First, strong states are likely to produce strong welfare states, with state strength defined in terms of governmental administrative capacities and institutional cohesion. Extensive administrative and financial resources make it easier to build expansive social policies.[27] Where political authority is fragmented, entrenched minorities will often block social legislation.[28] Federalism, separation of powers, strong bicameral-

[25] Peter Hall, *Governing the Economy* (Oxford: Oxford University Press, 1986); James March and Johan Olsen, *Rediscovering Institutions* (New York: Free Press, 1989); North (fn. 20).

[26] See, for example, Margaret Weir, Ann Shola Orloff, and Theda Skocpol, eds., *The Politics of Social Policy in the United States* (Princeton: Princeton University Press, 1988); and Theda Skocpol, *Protecting Soldiers and Mothers: The Political Origins of Social Policy in the United States* (Cambridge: Harvard University Press, 1992).

[27] Hugh Heclo, *Modern Social Politics in Britain and Sweden* (New Haven: Yale University Press, 1974).

[28] Keith G. Banting, *The Welfare State and Canadian Federalism*, 2d ed. (Montreal: McGill-Queen's University Press, 1987); Ellen Immergut, *Health Politics: Interests and Institutions in Western Europe* (Cambridge: Cambridge University Press, 1992).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ism or reliance on referenda all may restrict welfare state development. Although much of the work on institutions and welfare states has been based on comparative historical case studies, this claim about formal institutional veto points has recently received support in an important quantitative study as well.[29]

The second central institutional argument concerns policy legacies, or feedback—the consequences of previously introduced welfare state programs. Arguments about policy feedback are essentially arguments about the consequences of big government. As policy decisions have had increasingly pervasive effects on economic and social life, their impact on political processes has expanded. Given that the welfare state is at the very heart of big government, it should come as no surprise that studies of welfare state development have generated some of the most persuasive arguments about policy feedback.

The possible consequences of preexisting policy structures for welfare state politics are quite diverse.[30] Welfare state structures affect the size and orientation of various societal groups as well as patterns of interest-group formation. Programs may provide the basis for processes of social learning that affect prospects for future program expansion, whether negatively or positively. Policies can create long-term commitments—such as the pay-as-you-go intergenerational contracts common to public pension systems—that lock in particular paths of policy development.[31]

How easily can these arguments be applied to the distinctive politics of retrenchment? Again, there is no reason to assume that claims for earlier periods can simply be turned on their heads. For example, there is little reason to expect that bureaucratic capacities will be particularly important in an age of retrenchment. Can we administer it? may be an important question in a discussion of new or greatly expanded public initiatives, but for advocates of retrenchment the primary goal is to dismantle existing programs. Closing offices, curtailing services, and cutting benefits do not require formidable administrative capacity.

Arguments about the consequences of governmental cohesion also need to be reappraised in this new context.[32] At first glance, one might

[29] Huber, Ragin, and Stephens (fn. 1).

[30] Pierson (fn. 11).

[31] For examples of each of these arguments, see, respectively, Esping-Andersen (fn. 11); Skocpol (fn. 26); and Paul Pierson, "'Policy Feedbacks' and Political Change: Contrasting Reagan and Thatcher's Pension-Reform Initiatives," *Studies in American Political Development* 6 (Fall 1992).

[32] This paragraph relies on Paul Pierson and R. Kent Weaver, "Imposing Losses in Pensions Policy," in R. Kent Weaver and Bert Rockman, eds., *Do Institutions Matter? Government Capabilities at Home and Abroad* (Washington, D.C.: Brookings Institution, 1993).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

expect that systems with fewer institutional veto points would be in a stronger position to pursue an agenda of radical retrenchment. Because retrenchment is generally unpopular, however, there are compelling reasons to question this expectation. While cohesive systems concentrate authority, they also concentrate accountability. The former tendency facilitates retrenchment, but the latter impedes it. Where authority is centralized, the public knows that the government of the day can prevent groups from suffering cutbacks. Strong governments, anticipating the high political cost of retrenchment, may forgo the opportunities provided by concentrated power. Thus, the theoretical basis for believing that government cohesion facilitates retrenchment is weak. We are left with the empirical question of whether concentration of power effects outweighs concentration of accountability effects.[33]

The tremendous scope of modern welfare states suggests that institutionalist arguments about policy feedback may be even more relevant to the politics of retrenchment. There are, however, two quite different ways to apply policy feedback arguments to retrenchment. First, one could develop nuanced arguments that emphasize the distinctive characteristics of individual programs and their implications for successful retrenchment. Alternatively, one could present arguments about the overarching structures of particular welfare state regimes, suggesting that they are likely to promote a particular kind of politics.

The first approach has promise but is difficult to carry out in practice. Previous policies help shape the distribution of political resources. Preexisting policy designs may influence interest-group networks, the extent of long-term commitments, the rules governing programmatic reform, and the availability of techniques to reduce the visibility of cutbacks. These kinds of arguments have been used in qualitative case studies of both welfare state expansion and retrenchment.[34] Because they often apply to idiosyncratic characteristics of individual programs, however, it is hard to use them to generate general propositions about variations across countries.

The alternative of developing broad arguments about how welfare state regimes affect contemporary politics is more easily applied to cross-national comparisons. Esping-Andersen has developed propositions that link welfare state structures to cross-national variation in oc-

[33] What seems more likely is that the structure of formal institutions will influence the *strategies* of retrenchment advocates. I return to this point in the conclusion.

[34] On expansion, see Heclo (fn. 27); and Skocpol (fn. 26). On retrenchment, see Pierson (fn. 12).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

cupational structures and, in turn, to contemporary political cleavages.[35] He suggests, for example, that social democratic welfare states like Sweden will face growing clashes between public and private sector workers, while conservative welfare states like Germany will produce a divide between labor market "insiders" and "outsiders." Such an approach offers the tantalizing promise of linking the evident significance of large welfare state structures to clear propositions about political change. Unfortunately, the argument does not work. As I will document in the next section, the hypothesized political cleavages emerge in only muted forms and have failed to generate a sustained backlash against the welfare state. The flaw in these broad arguments about welfare state regimes is that they greatly underestimate the difficulty of assembling and sustaining proretrenchment coalitions.

*New institutionalist arguments have contributed greatly to our understanding* of welfare state politics. Moreover, unlike arguments about the role of organized labor, there is no reason to think that the importance of institutional structures and the legacies of previous policy choices has declined. These arguments cannot simply be transferred from one context to another, however; they must be recast to apply to the specific settings and strategic problems that are characteristic of retrenchment politics.

## From Theories of Expansion to Theories of Retrenchment

It is commonly maintained that our knowledge of welfare state expansion provides us with considerable insight into the new politics of the welfare state. Although this view is rarely stated explicitly, it undoubtedly explains why political scientists, who are usually preoccupied with understanding contemporary or rather recent events, have become so interested in historical studies of social policy. The presumed similarity of expansion and retrenchment is evident in some of the most important work on comparative social policy. In their sophisticated quantitative investigation of welfare state effort from 1956 to 1988, for example, Huber, Ragin, and Stephens acknowledge that their use of a pooled cross-sectional time-series model assumes "that causal processes are uniform through time." Esping-Andersen claims that "[t]he risks of

[35] Esping-Andersen (fn. 1); Gösta Esping-Andersen, "Postindustrial Cleavage Structures: A Comparison of Evolving Patterns of Social Stratification in Germany, Sweden, and the United States," in Francis Fox Piven, ed., *Labor Parties in Postindustrial Societies* (Oxford: Polity Press, 1991); and idem, "The Emerging Realignment between Labour Movements and Welfare States," in Marino Regini, ed., *The Future of Labour Movements* (London: Sage, 1992).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

welfare-state backlash depend . . . on the class character of welfare states. . . . [T]he class coalitions in which the three welfare-state regime-types were founded, explain not only their past evolution but also their future prospects." More generally, he maintains that "a theory that seeks to explain welfare-state growth should also be able to understand its retrenchment or decline."[36]

I see no reason to believe that this is true. Retrenchment is not simply the mirror image of welfare state expansion. Why should we assume that theories designed to explain outcomes in a particular context and involving the pursuit of particular goals will still apply once the political environment and the goals of key actors have undergone radical change? The question of whether theories of welfare state expansion offer insights into the retrenchment process is still open, but this preliminary discussion suggests that major modifications are probably required. In the following section, I draw on evidence from Great Britain, the United States, Germany, and Sweden to demonstrate the distinctiveness of retrenchment politics. Of declining importance are some formerly critical factors, such as the role of organized labor. Others, such as the design of political institutions, are of continuing significance but in new ways. Yet a crucial emerging factor is the mature welfare state itself, and its broad and deep reservoirs of public support.

## III. Retrenchment Politics in Four Countries

To what extent have welfare states undergone retrenchment? What countries and programs have been most vulnerable to retrenchment initiatives and why? In this section I address these questions by reviewing the evolution of welfare states in four affluent democracies since the late 1970s. The evidence supports a number of claims. (1) There is little evidence for broad propositions about the centrality of strong states or left power resources to retrenchment outcomes. (2) The unpopularity of retrenchment makes major cutbacks unlikely except under conditions of budgetary crisis, and radical restructuring is unlikely even then. (3) For the same reason, governments generally seek to negotiate consensus packages rather than to impose reforms unilaterally, which further diminishes the potential for radical reform. And (4) far from creating a self-reinforcing dynamic, cutbacks tend to replenish support for the welfare state.

[36] Huber, Ragin, and Stephens (fn. 1), 733; Esping-Andersen (fn. 1), 33, 32. Of course, Esping-Andersen has also emphasized that the growth of the welfare state affects welfare state politics.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Measuring retrenchment is a difficult task. Quantitative indicators are likely to be inadequate for several reasons. First, pure spending levels are rarely the most politically important or theoretically interesting aspects of welfare states. As Esping-Andersen put it in his analysis of welfare state expansion, "It is difficult to imagine that anyone struggled for spending per se."[37] In particular, rising unemployment may sustain high spending even as social rights and benefits are significantly curtailed. Second, spending estimates will fail to capture the impact of reforms that are designed to introduce retrenchment only indirectly or over the long term. Analysis must focus on qualitative and quantitative changes in programs and on prospective, long-term changes, as well as on immediate cutbacks. My investigation therefore relies on a combination of quantitative data on expenditures and qualitative analysis of welfare state reforms.[38] Rather than emphasizing cuts in spending per se, the focus is on reforms that indicate structural shifts in the welfare state. These would include (1) significant increases in reliance on means-tested benefits; (2) major transfers of responsibility to the private sector; and (3) dramatic changes in benefit and eligibility rules that signal a qualitative reform of a particular program.[39] The selection of countries to investigate was based on the desire to achieve significant variation on what the welfare state expansion literature suggests are the most plausible independent variables. The cases vary widely in the structure of political institutions, the extent of shifts in the distribution of power resources, the design of preexisting welfare states, and the severity of budgetary crisis.

Beginning with the quantitative evidence, aggregate measures provide little evidence that any of the four welfare states have undergone dramatic cutbacks. From 1974 through 1990 the expenditure patterns across the four cases are quite similar, despite widely different starting

[37] Esping-Andersen (fn. 1), 21.

[38] A recent draft paper by Stephens, Huber, and Ray presents the first sophisticated statistical analysis of retrenchment, utilizing newly assembled data that allow investigation of fairly detailed programmatic changes over a large number of countries. There are important limitations: much of the programmatic data end in 1986 or 1987; many programs are not covered; and the still-small sample allows the statistical testing of only a few broad hypotheses (essentially, the impact of partisanship) about the politics of program change. The results reported strongly support most of the analysis presented here, although they view Thatcher as more successful than I do. John D. Stephens, Evelyne Huber, and Leonard Ray, "The Welfare State in Hard Times" (Paper presented at the conference on the "Politics and Political Economy of Contemporary Capitalism," University of North Carolina, Chapel Hill, September 1994).

[39] Establishing what constitutes "radical" reform is no easy task. For instance, it is impossible to say definitively when a series of quantitative cutbacks amounts to a qualitative shift in the nature of programs. Roughly though, that point is reached when because of policy reform a program can no longer play its traditional role (e.g., when pension benefits designed to provide a rough continuation of the retiree's earlier standard of living are clearly unable to do so).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

points. As Tables 1 and 2 show, social security spending and total government outlays as a percentage of GDP are relatively flat over most of the relevant period. The exception is the recent surge in Swedish expenditures, which will be discussed below. There is a slight upward trend overall, with fluctuations related to the business cycle. Table 3, which tracks public employment, reveals a similar pattern (although the expansion of Swedish public employment from an already high base stands out). For none of the countries does the evidence reveal a sharp curtailment of the public sector.

Table 4 offers more disaggregated indicators of shifts in social wel-

TABLE 1
SOCIAL SECURITY TRANSFERS AS % OF GDP
(1974–90)

| | *Britain* | *Germany* | *Sweden* | *United States* |
|---|---|---|---|---|
| 1974 | 9.8 | 14.6 | 14.3 | 9.5 |
| 1980 | 11.7 | 16.6 | 17.6 | 10.9 |
| 1982 | 14.0 | 17.7 | 18.3 | 11.9 |
| 1984 | 14.0 | 16.5 | 17.6 | 11.0 |
| 1986 | 14.1 | 15.9 | 18.4 | 11.0 |
| 1988 | 12.3 | 16.1 | 19.5 | 10.6 |
| 1990 | 12.2 | 15.3 | 19.7 | 10.8[a] |

SOURCE: OECD, *Historical Statistics, 1960–1990* (1992), table 6.3.
[a] 1989.

TABLE 2
GOVERNMENT OUTLAYS AS % OF NOMINAL GDP
(1978–94)

| | *Britain* | *Germany* | *Sweden* | *United States* |
|---|---|---|---|---|
| 1978 | 41.4 | 47.3 | 58.6 | 30.0 |
| 1980 | 43.0 | 47.9 | 60.1 | 31.8 |
| 1982 | 44.6 | 48.9 | 64.8 | 33.9 |
| 1984 | 45.2 | 47.4 | 62.0 | 32.6 |
| 1986 | 42.5 | 46.4 | 61.6 | 33.7 |
| 1988 | 38.0 | 46.3 | 58.1 | 32.5 |
| 1990 | 39.9 | 45.1 | 59.1 | 33.3 |
| 1992 | 43.2 | 49.0 | 67.3 | 35.1 |
| 1994[a] | 44.8 | 51.4 | 70.9 | 33.9 |

SOURCE: OECD, *Economic Outlook* (December 1993), table A23.
[a] Projection.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

TABLE 3
GOVERNMENT EMPLOYMENT AS % OF TOTAL EMPLOYMENT
(1974–90)

| | *Britain* | *Germany* | *Sweden* | *United States* |
|---|---|---|---|---|
| 1974 | 19.6 | 13.0 | 24.8 | 16.1 |
| 1980 | 21.1 | 14.6 | 30.3 | 15.4 |
| 1982 | 22.0 | 15.1 | 31.7 | 15.4 |
| 1984 | 22.0 | 15.5 | 32.6 | 14.8 |
| 1986 | 21.8 | 15.6 | 32.2 | 14.8 |
| 1988 | 20.8 | 15.6 | 31.5 | 14.4 |
| 1990 | 19.2 | 15.1 | 31.7 | 14.4[a] |

SOURCE: OECD, *Historical Statistics, 1960–1990* (1992), table 2.13
[a] 1989.

fare spending among the four countries; spending patterns are reported for what the OECD terms "merit goods" (primarily housing, education, and health care) as well as for various income transfers. The figures suggest a bit more divergence among the cases, with the United States and Germany emerging as somewhat more successful in curbing spending. A very few program areas—notably British housing and German pensions—experienced significant reductions. Nonetheless, similarities across countries remain more striking than differences. None of the cases show major rises or declines in overall effort, and there are few indications of dramatic change in any of the subcategories of expenditure.

The data suggest a surprisingly high level of continuity and stability.[40] These figures must be treated with caution, however, since major changes in the spending for particular programs could be occurring within these broad categories. Policy reforms could have imposed lagged cutbacks that do not show up in spending figures. Furthermore, many other features of programs, not just spending levels, are of significance. To investigate these issues and to get a better sense of the processes that generated these aggregate outcomes, we turn to a more detailed investigation of the four cases.

## GREAT BRITAIN

By the mid-1970s Britain had developed a midsize welfare state with a mix of fairly modest income transfer programs and relatively extensive

[40] This broad conclusion is echoed for a much larger number of cases in Stephens, Huber, and Ray (fn. 38).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

TABLE 4
GOVERNMENT OUTLAYS BY FUNCTION AS % OF TREND GDPA[a]
(1979–90)

| | *Britain* | | | *Germany* | | | *Sweden* | | | *United States* | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1979 | 1990 | 1979–90 | 1979 | 1990 | 1979–90 | 1979 | 1990 | 1979–90 | 1979 | 1989 | 1979–89 |
| Total | 44.9 | 43.2 | −1.7 | 49.9 | 45.8 | −4.1 | 63.2 | 61.4 | −1.8 | 33.2 | 36.9 | +3.6 |
| Public goods[b] | 9.5 | 9.7 | +0.1 | 10.0 | 9.2 | −0.8 | 10.5 | 8.8 | −1.7 | 8.2 | 9.3 | +1.1 |
| Merit goods | 13.6 | 12.2 | −1.4 | 12.3 | 10.9 | −1.4 | 15.9 | 13.4 | −2.6 | 6.1 | 6.0 | −0.1 |
| Education | 5.5 | 5.0 | −0.5 | 5.2 | 4.2 | −1.0 | 6.6 | 5.6 | −1.0 | 4.7 | 4.7 | −0.0 |
| Health[c] | 4.8 | 5.1 | +0.3 | 6.3 | 6.0 | −0.3 | 8.1 | 6.9 | −1.1 | 0.9 | 0.9 | −0.0 |
| Housing and other | 3.4 | 2.1 | −1.2 | 0.8 | 0.7 | −0.1 | 1.2 | 0.8 | −0.4 | 0.5 | 0.4 | −0.1 |
| Income Trans. | 12.5 | 13.4 | +0.9 | 20.2 | 18.5 | −1.7 | 24.6 | 26.8 | +2.2 | 11.2 | 11.9 | +0.7 |
| Pensions | 6.7 | 6.5 | −0.2 | 12.7 | 11.2 | −1.5 | 11.0 | 11.5 | +0.4 | 6.9 | 7.0 | +0.1 |
| Sickness | 0.4 | 0.3 | −0.1 | 0.8 | 0.7 | −0.1 | 3.4 | 4.5 | +1.2 | 0.1 | 0.2 | +0.1 |
| Family allow. | 1.7 | 1.6 | −0.0 | 1.2 | 0.8 | −0.4 | 1.6 | 1.3 | −0.3 | 0.4 | 0.4 | −0.0 |
| Unemployment | 0.7 | 0.6 | −0.1 | 0.9 | 1.3 | +0.4 | 0.4 | 0.5 | +0.1 | 0.4 | 0.3 | −0.1 |
| Other income supports | 0.1 | 0.8 | +0.7 | 1.3 | 1.6 | +0.3 | 0.1 | 0.2 | +0.1 | 0.0 | 0.0 | 0.0 |
| Admin. and other spend. | 1.4 | 1.6 | +0.3 | 2.6 | 2.4 | −0.2 | 4.9 | 5.2 | +0.3 | 0.6 | 0.6 | −0.0 |
| Add. transfer | 1.4 | 1.8 | +0.5 | 0.5 | 0.4 | −0.1 | 3.2 | 3.7 | +0.6 | 2.7 | 3.5 | +0.8 |

Source: OECD, *Economic Outlook* (December 1993), table 21.

[a] Numbers may not sum to total due to rounding.

[b] Defense and other public services.

[c] For the U.S., social security related to health spending is included under "additional transfers" below.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

and interventionist policies in health care and housing. The past fifteen years of Conservative rule represent a powerful test of a number of claims about retrenchment. There are few if any cases within the OECD of such a radical swing to the right in the distribution of power resources. A balanced two-party system gave way to Conservative hegemony, as reflected in four consecutive electoral victories.[41] A fairly strong labor movement suffered repeated defeats in the face of high unemployment and changes in industrial relations law; union density declined from over 55 percent in 1979 to 35 percent in 1993.[42] Furthermore, Britain's Westminster political system concentrates political authority. If a strong state with few internal veto points is the key to reforming the contemporary welfare state, the British Conservatives were in an unusually favorable position. In short, a simple inversion of welfare state expansion arguments would suggest that Britain should have been fertile ground for social policy cutbacks. The evidence does not support such a conclusion.[43] While there are individual instances of significant retrenchment, notably in housing and pensions policy, these are the exception rather than the rule. The British welfare state, if battered, remains intact. As Table 4 indicates, social expenditure (merit goods plus transfers) as a share of GDP remains almost unchanged after more than a decade of Conservative governance.

It is worth starting with the two cases of retrenchment success, because these experiences are instructive. One of the triumphs of the Thatcher government was the privatization of public council housing. The sale of roughly 1.5 million homes to tenants laid the foundation for a major expansion of home ownership and sharp cutbacks in subsidies for those who remained in the public sector.[44] Housing reform was a uniquely popular case of retrenchment—in many respects, the exception that proves the rule. The liquidation of extensive public sector assets created a rare opportunity for credit claiming rather than blame avoidance, offering considerable benefits for both home purchasers and taxpayers. Public sector tenants, who under other circumstances would have fought the government, became disinterested or divided.

[41] Geoff Garrett, "The Politics of Structural Reform: Swedish Social Democracy and Thatcherism in Comparative Perspective," *Comparative Political Studies* 25 (January 1993).

[42] The 1979 figure is from Robert Price and George Sayers Bain, "Union Growth in Britain: Retrospect and Prospect," *British Journal of Industrial Relations* 21 (March 1983), 47. The 1993 figure is from Derek Bird and Louise Corcoran, "Trade Union Membership and Density, 1992–93," *Employment Gazette* (June 1994), 193.

[43] Pierson (fn. 12), chaps. 3–6.

[44] Ray Forrest and Alan Murie, *Selling the Welfare State: The Privatization of Public Housing* (London: Routledge, 1988).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

The government's pension reforms were also relatively successful.[45] A less generous indexation rule for the basic pension produced gradual but considerable budgetary savings. The government also introduced significant cutbacks in the State Earnings-Related Pension Scheme (SERPS), while introducing a private personal pension alternative. The government's initial proposal—to abolish SERPS with a very limited phase-in period—met with overwhelming opposition, even from usual supporters like the Confederation of British Industry (CBI). Forced into an embarrassing retreat, the government introduced more modest but nonetheless substantial changes in SERPS, which will gradually expand private pensions while reducing public sector benefits. These changes, though criticized, failed to generate the kind of outcry that often led the government to back off from other reforms. Offering the carrot of personal pensions diminished the pain of the cuts in public pensions (although the required tax incentives also diminished the government's budgetary savings). More important, the government's use of incremental and seemingly technical reforms limited the emergence of opposition.

Careful political planning in the context of programs that were either weakly institutionalized (SERPS) or offered rare opportunities for credit claiming (council housing) protected the Thatcher government. These cases were exceptions, however. On the whole, the British Conservatives found the welfare state to be a political minefield, as popular support for social spending remained strong. In fact, British public opinion regarding social policy reveals the same pattern found elsewhere: a modest decline of support for the welfare state preceded the arrival of the Thatcher government but rebounded at the first hint of serious retrenchment. Public opinion in Britain has run strongly, and increasingly, in favor of maintaining or even expanding social provision.[46]

Thus while the government was clearly hostile to much of the welfare state and had the political authority to implement dramatic changes if it chose to do so, the fear of being held accountable for unpopular initiatives held it in check. Preserving the National Health Service, for example, became far and away the Labour Party's best issue in the 1980s. Initial exploration of various options for privatization provoked public outrage. The Thatcher government repeatedly backed off

[45] Alan Walker, "Thatcherism and the New Politics of Old Age," in John Myles and Jill Quadagno, eds., *States, Labor Markets, and the Future of Old Age Policy* (Philadelphia: Temple University Press, 1991); Pierson (fn. 31).

[46] Peter Taylor-Gooby, "The Future of the British Welfare State: Public Attitudes, Citizenship and Social Policy under the Conservative Governments of the 1980s," *European Sociological Review* 4 (May 1988).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

from plans for fundamental restructuring of the system.[47] By the end of the decade the government's repeated promise had become "the NHS is safe with us."

While the government achieved some nontrivial incremental cutbacks in various programs, radical retrenchment efforts failed, often at considerable political cost. The universal Child Benefit, frequently rumored to be in jeopardy, survived (although at a somewhat reduced level), due in part to well-organized lobbying efforts. A massive and highly publicized social security review promising to offer a "new Beveridge" ended up making modest adjustments to programs for low-income groups.[48] Sickness Pay, touted as an instance of successful privatization, remains a thinly disguised public sector benefit.[49] Furthermore, attempts to foster retrenchment arguably caused Thatcher's ultimate downfall. The tremendously unpopular poll tax—designed to cripple the social spending of local governments by cutting their financial legs out from under them—was a major source of the downward spiral in the polls that forced Thatcher's resignation. Her successor, John Major, followed a more moderate course. While attempting to consolidate Thatcher's least unpopular reforms, he launched few initiatives of his own and retreated on unpopular issues like cutbacks in Child Benefit.

Parts of the Conservative record demonstrate that major retrenchment is not impossible. Where a government can obscure the consequences of reform—or better yet, turn reform into a source of tangible benefits—the welfare state may be vulnerable. Had the entire British welfare state resembled council housing, the Conservative agenda would have succeeded. Yet the government's record reveals more cases of incremental adjustments or failed attempts to restructure programs. Overall social expenditure remains almost unchanged; housing and pensions aside, the government paid a significant price for the cutbacks it was able to impose. This outcome stands in sharp contrast to the Thatcher government's remarkably successful efforts in other policy areas, such as its overhaul of Britain's industrial relations system and its privatization of publicly owned industries.

[47] Rudolf Klein, *The Politics of the National Health Service*, 2d ed. (London: Longman, 1989); Edwin Griggs, "The Politics of Health Care Reform in Britain," *Political Quarterly* 62 (October–December 1991).

[48] Nicholas Deakin, *The Politics of Welfare* (London: Methuen, 1987).

[49] Nicholas Barr and Fiona Coulter, "Social Security: Solution or Problem?" in John Hills, ed., *The State of Welfare: The Welfare State in Britain since 1974* (Oxford: Oxford University Press, 1990), 281; Michael O'Higgins, "Social Welfare and Privatization: The British Experience," in Sheila B. Kamerman and Alfred J. Kahn, eds., *Privatization and the Welfare State* (Princeton: Princeton University Press, 1989).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## The United States

Many have seen the United States as another likely candidate for a dismantling of the welfare state. Like Britain, the United States experienced a significant rightward shift in power resources during the 1980s. Republicans captured the presidency in 1980 (as well as the Senate until 1986). Union power—never that extensive to begin with—continued a seemingly inexorable decline. The American welfare state was already fairly modest in scope, suggesting to some observers that public support for maintaining it would be weak. Unlike Thatcher, however, retrenchment advocates in the United States operated in a context of severely fragmented political authority. The combination of weak parties, separation of powers, and federalism created an institutional environment that was in many respects the polar opposite of that in Britain.

Yet at least through 1994 the American story reads like the British one, minus most of Thatcher's sporadic successes. Reagan's first year was the exception. Riding the antitax wave that had helped to elect him, Reagan was able to cobble together a loose coalition of southern Democrats and Republicans in his first year to pass some cuts in social programs, especially those affecting the poor. A decade-long expansion of low-income housing programs was rapidly reversed. Significant cuts were introduced in the main program for the poor, AFDC, and in Unemployment Insurance. The Reagan administration successfully exploited the fact that responsibility for these two programs was shared with fiscally strapped state governments. Both fared poorly in the 1980s, although many of the cutbacks occurred at the state level.[50]

This first-year record has shaped many appraisals of the Reagan revolution.[51] As in other countries, however, popular support for retrenchment dissipated rapidly. The Reagan assault petered out in 1982, when further budget cuts were overwhelmingly rejected. Reagan's single major reform initiative, the New Federalism proposal, would have transferred responsibility for AFDC and food stamps to the states (in return for the federal government's assumption of complete control over

[50] In the case of AFDC, which is not indexed, this happened largely because state governments failed to index benefits to inflation. Given this structural feature of the program, "nondecisions" allowed quiet retrenchment. This trend predated Reagan's arrival in office. Indeed, cuts in real benefits were greater during Carter's presidency (when inflation was high) than under Reagan.

[51] See, for example, two frequently cited studies: Sara A. Rosenberry, "Social Insurance, Distributive Criteria and the Welfare Backlash: A Comparative Analysis," *British Journal of Political Science* 12 (October 1982); and John Palmer and Isabel Sawhill, eds., *The Reagan Experiment* (Washington, D.C.: Urban Institute Press, 1982).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Medicaid). The proposal was so unpopular, however, that it could not find even a single congressional sponsor and died without ever being introduced.[52] By Reagan's second term incremental expansions of various social programs for the poor were back on the agenda, and Congress passed modest increases in food stamps and Medicaid and a dramatic expansion of the earned income tax credit for poor working families.[53]

Middle-class programs also weathered the storm. Trust fund difficulties forced significant reforms of Social Security, and there was a series of efforts to trim Medicare's exploding costs (mostly through cuts in provider compensation). In all these efforts, however, Republicans fearful of the electoral consequences of retrenchment refused to move forward in the absence of bipartisan agreement. The need for consensus in turn assured that reforms would be acceptable to program defenders within the Democratic Party. This was most clearly evident in the 1983 Social Security amendments, where the reliance on a bipartisan, quasi-corporatist commission assured that radical reforms would be rejected.[54] It was also true, however, of the series of broad budget packages that sought cutbacks in the Medicare system.[55]

Although it is generally argued that the residual nature of the welfare state in the United States creates a narrow political base, the initial backlash against the welfare state was short-lived. Declining support for social programs *preceded* Reagan's election. From 1982 onward—that is, immediately following the first round of budget cuts—polls revealed growing support for the welfare state.[56] As is true elsewhere, support for means-tested programs was far lower than that for middle-class programs, but the same public opinion pattern of modest declines in support followed by rapid recovery is evident for both targeted and universal programs. Reagan became much more hesitant as popular enthusiasm for retrenchment faded. In any event, the fragmented nature

[52] Tim Conlan, *New Federalism: Intergovernmental Reform from Nixon to Reagan* (Washington, D.C.: Brookings Institution, 1988), 95–238.

[53] Paul E. Peterson, "The Rise and Fall of Special Interest Politics," *Political Science Quarterly* 105 (Winter 1990–91); Robert Greenstein, "Universal and Targeted Approaches to Relieving Poverty," in Christopher Jencks and Paul Peterson, eds., *The Urban Underclass* (Washington, D.C.: Brookings Institution, 1991).

[54] Paul Light, *Artful Work: The Politics of Social Security Reform* (New York: Random House, 1985).

[55] Joseph White and Aaron Wildavsky, *The Deficit and the Public Interest* (Berkeley: University of California Press, 1989).

[56] Fay Lomax Cook and Edith J. Barret, *Support for the American Welfare State* (New York: Columbia University Press, 1992); Robert Y. Shapiro and John T. Young, "Public Opinion and the Welfare State: The United States in Comparative Perspective," *Political Science Quarterly* 104 (Spring 1989). In line with my general argument, Shapiro and Young's research indicates similar patterns in other countries.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

of American political institutions assured that plans for further cutbacks met a hostile reception in Congress.

To be sure, with both the emergence of a large structural budget deficit during the 1980s and resistance to tax increases, little room was left for social policy expansion. The American welfare state moved into a zero-sum era, in which gains for some programs often came at the expense of others. This atmosphere continued when the Democrats returned to the White House in 1992, although social spending for the poor was a prime beneficiary of the 1993 budget agreement. From the late 1980s through 1994 the situation was one of reallocation within an essentially stagnant budget.[57]

The 1994 elections, which ended forty years of Democratic predominance in Congress, precipitated the most vigorous challenge yet to the American welfare state. Republicans had learned important lessons from past defeats. Social Security was taken off the table. The issue was carefully framed as a matter of controlling the deficit and bringing government "closer to the people." Efforts at institutional change (the line-item veto and balanced-budget amendment) preceded (though with limited success) attacks on social programs. To diminish visibility, most of the major cuts were scheduled for the year 2000 and beyond. If fully implemented, the Republican budget proposals introduced in 1995 would represent a fundamental reform of American social policy. It will, however, be several years before the outcome of this latest battle is clear. Republican cutbacks are only now being formulated, and it will take some time for their impact to register with the electorate. While the current political environment poses a major test of the resilience of the welfare state, both American precedent and the experience elsewhere cast doubt on the proposition that Republicans will discover a deep reservoir of public tolerance for sharp cuts in social programs.

## GERMANY

Germany, like Sweden, has a very extensive welfare state, though the German system is geared toward transfer payments rather than public services, and toward redistribution over the life cycle rather than across income groups. As in Britain and the United States, there has been a considerable swing to the right in elections during the period of austerity. A right-of-center coalition has been in office since 1982. In recent

[57] On recent spending trends, see House Ways and Means Committee, *Background Material on Programs within the Jurisdiction of the Committee on Ways and Means* (Washington, D.C.: GPO, March 1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

years, however, the Social Democrats, with their majority in the Bundesrat, have gained considerable influence. And although Germany's powerful unions have been under pressure, compared with unions in other countries their organizational strength has held up quite well.[58] Thus, Germany represents a case of moderately diminished left power resources and relatively fragmented political authority.

The German welfare state is based, not on maximizing employment, but on providing subsidies to the "outsiders," who are encouraged to leave the labor market to those who are highly productive. Esping-Andersen has speculated that the result is likely to be an "insider-outsider" conflict in which the employed (along with employers) increasingly balk at the cost of subsidizing a large and growing "surplus population."[59] Indeed, within the recent wave of commentary about the contribution of high wages and extensive social protection to Europe's economic problems, Germany's huge wage costs (including steeply rising payroll taxes) have received particular attention.[60] Adding to the stress has been the cost of unification, as the West German welfare state was extended to cover the far less productive East Germany.

The fiscal pressures facing Germany are evident and are unlikely to go away. Demographic shifts will increase costs even if expenses related to unification begin to subside. There is, however, little sign that these pressures will translate into a sharp insider/outsider conflict. This line of potential cleavage is based largely on age, with by far the largest and most expensive group of outsiders consisting of former insiders: pensioners and early retirees. There are formidable barriers to the development of political cleavages along generational lines.[61] Where costs associated with aging are the main source of budgetary pressure, insiders will have to recognize that in the future they too will be outsiders. This is likely to temper any tendency toward a polarization between "them" and "us."[62]

Far from revealing a sharp new political cleavage, the reform of pensions in the late 1980s fits the general cross-national pattern for re-

[58] Thelen (fn. 19).

[59] Esping-Andersen (fn. 35, 1991 and 1992).

[60] Combined employer and employee social insurance contributions were 26.5% of gross income in 1970, 32.4% in 1980, and are forecast to hit 39.2% in 1994. *Financial Times*, July 2, 1993, p. 13.

[61] Hugh Heclo, "Generational Politics," in John L. Palmer, Timothy Smeeding, and Barbara Boyle Torrey, eds., *The Vulnerable* (Washington, D.C.: Urban Institute Press, 1988).

[62] Esping-Andersen (fn. 35, 1992) rightly suggests that the development of private pension schemes could encourage such a polarization, since it would allow current workers to sever the link between their own retirement situation and that of the preceding generation. Yet the enormous institutional and political barriers to any radical change in a mature, pay-as-you-go pension system make a major development along these lines highly unlikely. See Pierson (fn. 31).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

trenchment in popular social programs.[63] With projections indicating enormous long-term deficits as a result of demographic trends, the need for pension reform was widely recognized. While some critics pressed for a rethinking of the entire scheme, the Kohl government instead searched for consensus among experts and the social partners, and eagerly sought support from the opposition Social Democrats. Union and business representatives submitted joint statements on pension reform. All parties except the Greens supported the Pension Reform Act passed in November 1989.[64] The resulting plan incorporated familiar pruning techniques: slightly lower replacement rates, an increase in the retirement age, and increased contributions. Combined with earlier cutbacks, these reforms have generated substantial budgetary savings. The basic structure of Germany's generous pension system remained unaltered, however. In the case of health care reform as well, corporatist accommodation of entrenched interests and a search for cross-party consensus has been the rule.[65]

The one indication of a distinctly conservative cast to retrenchment initiatives prior to 1989 came in the pattern of benefit cuts. Most affected were welfare and unemployment insurance benefits that could be considered a hindrance to labor market flexibility. While these benefits were relatively well protected under the SPD-led coalition of the late 1970s, they experienced disproportionate reductions after 1982.[66] Still, the differences were limited and did not overturn the basic reality that social welfare policy operated within a relatively consensual framework. As Offe has argued, moderate cutbacks were carefully designed by a "*de facto* bipartisan coalition" and orchestrated to prevent a political outcry.[67]

The strains of the postunification period raised the possibility of more dramatic reform. Germany's worsening fiscal situation, combined with concern about industrial competitiveness, generated growing crit-

[63] Karl Hinrichs, "Public Pensions and Demographic Change: Generational Equity in the United States and Germany," Centre for Social Policy Research Working Paper no. 16/93 (Bremen: University of Bremen, 1993); Winifried Schmähl, "Die Finanzierung der Rentenversicherung im vereinten Deutschland," *Wirtschaftsdienst*, no. 1 (1992).

[64] Friedbert Rüb and Frank Nullmeier, "Altersiccherungspolitik in der Bundesrepublik," in Berhard Blanke and Hellmut Wollmann, eds., *Die alte Bundesrepublik: Kontinuität und Wandel* (Opladen: Westdeutscher Verlag, 1991).

[65] Douglass Webber, "Krankheit, Geld und Politik: Zur Geschichte der Gesundheitsreform in Deutschland," *Leviathan* 16 (1988).

[66] Jens Alber, "The West German Welfare State in Transition," in R. Morris, ed., *Testing the Limits of Social Welfare* (Hanover: Brandeis University Press, 1988); Claus Offe, "Smooth Consolidation in the West German Welfare State: Structural Change, Fiscal Policies, and Populist Politics," in Piven (fn. 35).

[67] Offe (fn. 66), 140.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

icism of the welfare state. Yet the response to unification emphasized continuity: East Germans were brought into the West German social policy regime on extremely generous terms. In response to budgetary pressures since then, a series of cuts have been introduced in major social programs, and more cuts are probably on the way.[68] Again, however, the pattern has been to trim benefit levels rather than challenge the basic structure of programs.

The recent ambitious expansion of long-term care covering in-home and nursing-home services is clear grounds for skepticism about the prospects for radical retrenchment or a generational backlash against the German welfare state.[69] The system will relieve the sickness funds and local social assistance budgets of responsibility for long-term care expenditures. While the scheme partly amounts to fiscal relief for strapped *Länder* (state) governments, it involves significant new benefits as well. Its introduction at a time of budgetary stress and widespread discussion of high social wage costs indicates the continuing political attractiveness of social programs, as well as the electoral clout of the elderly.[70]

There is a possibility that groups more easily defined as problem cases, such as the long-term unemployed (especially disaffected youth, immigrants, or East Germans) could become the targets for political attacks. Concern about mounting unemployment rates and labor market inflexibilities point in the same direction. The Kohl government's recent proposals for cuts in social expenditures do indeed concentrate on unemployment and welfare benefits. Sharp cuts, however, will provoke a strong challenge from the SPD and unions, since the conditions of the unemployed have significant implications for workers. Furthermore, the force of demographic demands is such that even these politically difficult reforms would have only a limited effect on the long-term budgetary situation.[71] The recent history of retrenchment suggests that most governments are likely to be skittish about pursuing

[68] Jürgen Plaschke, "Die Sozialpolitik in den Monaten November, Dezember 1993 und ein sozialpolitischer Rückblick auf das Jahr 1993," *Nachrichtendienst*, no. 2 (1994).

[69] Jens Alber, "The Debate over Long-Term Care Insurance in Germany" (Contribution to an OECD seminar on the Care of the Elderly, Paris, OECD, 1994); Ulrike Götting, Karin Haug, and Karl Hinrichs, "The Long Road to Long-Term Care Insurance in Germany: A Case Study in Welfare State Expansion" (Paper presented at the World Congress of Sociology, Bielefeld, July 1994).

[70] Tyll Necker, president of the Association of German Industry (BDI), described the original proposal (which did not include the reduction of one paid holiday as an offset) as an official declaration of war against German industry. Alber (fn. 69), 17.

[71] By 2040 pensions are expected to account for 61% of German social expenditure, compared with 40% in Britain and 44% in Sweden. OECD, *Aging Populations: The Social Policy Implications* (Paris: OECD, 1988).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

big social policy battles unless they promise to yield substantial budgetary gains.

Demographic and budgetary pressures assure that an atmosphere of austerity will continue to surround the German welfare state. Indeed, the German government has been quite successful in holding the line on spending. Yet, as Offe aptly puts it, it has been a period of "smooth consolidation." A fundamental rethinking of social policy seems a remote possibility. The structure of political institutions—both constitutional rules and corporatist policy networks—puts a premium on consensus. The SPD's significant gains in the October 1994 elections, where Kohl's coalition government retained only a razor-thin majority, are unlikely to invigorate a governing coalition that has never shown much appetite for radical initiatives.

## Sweden

Sweden combines a tremendously successful social democratic party, powerful unions, and one of the world's most extensive and redistributive welfare states. With the breakdown of centralized collective bargaining, union power has weakened in the past decade, and the political hegemony of the SAP has given way to periodic fluctuations between SAP governance and coalitions of the bourgeois parties.[72] Swedish institutions, like British ones, provide for a considerable concentration of political authority.

As with Germany, an analysis of trends in Swedish social policy must distinguish two periods—the cyclical patterns that Sweden shared with other countries prior to 1990 and the dramatic worsening of economic and budgetary circumstances over the past four years. Despite the distinctiveness of Swedish politics and the Swedish welfare state, the dynamics of reform prior to 1990 bears many similarities to the processes discussed in the three preceding cases. Regardless of who was in office, there was only occasional trimming of social programs; no government showed much enthusiasm for a major revamping of the Swedish welfare state.

Esping-Andersen has tried to link the prospects for retrenchment to policy feedback from the structure of Sweden's welfare state, positing that Sweden's system of extensive service provision and high public sector employment promotes a cleavage between workers in the public and

[72] A bourgeois coalition government was in power from 1976 to 1982 and, following the SAP's worst showing in decades in the "earthquake" election of 1991, from 1991 to 1994.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

private sectors.[73] In the 1980s both private sector unions and employers criticized public employees. This occurred in part because of the way Sweden's centralized industrial relations system created linkages between public and private sector pay, and in part simply because of the high tax costs of massive public sector employment expansion.[74]

It might be expected that the events of the past few years would exacerbate this tension. The Swedish economy came under extraordinary pressure after 1990. The fall in output and the rise in unemployment seem to have had relatively little to do with the welfare state itself.[75] Yet if the welfare state did not cause the economic crisis, it is clearly implicated in Sweden's current predicament. Unemployment, including those participating in government-financed active labor market schemes, rose from 3 percent in 1989 to over 12 percent in 1993.[76] Designed to operate at full employment, the Swedish welfare state cannot tolerate burdens of this magnitude. Sweden's generous and expensive social benefits led to immediate fiscal trouble when rising unemployment produced falling revenues and higher outlays. In only four years Sweden went from having the largest surplus in the OECD to operating the largest deficit. Government outlays reached the extraordinary level of 73 percent of GDP in 1993, and the deficit stood at over 14 percent of GDP.[77] Given existing levels of taxation, the adjustment burden was bound to fall heavily on the expenditure side.

The emergence of a true fiscal crisis after 1990 required extensive reforms. Furthermore, between 1991 and 1994 Sweden was governed by a bourgeois coalition—and one whose center of gravity was considerably to the right of the one that governed between 1976 and 1982. Conditions thus might have seemed uniquely favorable to a complete overhaul of social policy. What is striking is that even under these extraordinary circumstances there was no sign that the welfare state would be radically restructured. Instead, considerable care was taken to operate within the structure of existing programs.[78] Prominent ex-

[73] Esping Andersen (fn. 1); Esping-Andersen (fn. 35, 1992); see also Peter Swenson, "Labor and the Limits of the Welfare State," *Comparative Politics* 23 (July 1991).

[74] Schwartz (fn. 15); Pontusson and Swenson (fn. 19).

[75] OECD, *Economic Survey: Sweden* (Paris: OECD, 1994); Evelyne Huber and John Stephens,"The Future of the Social Democratic Welfare State" (Paper presented at the International Sociological Association Meeting, Oxford, September 1993), 7–11.

[76] OECD (fn. 75), 36.

[77] Ibid.

[78] John D. Stephens, "The Scandinavian Welfare States: Development and Crisis" (Paper presented at the World Congress of Sociology, Bielefeld, Germany, July 1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

amples include an expansion of waiting days for unemployment and sickness benefits, a lowering of replacement rates for unemployment benefits (from 90 percent to 80 percent), a freeze on adjustments in child allowances, and a raise in the retirement age, from sixty-five to sixty-six.

Ironically, the breakdown of other components of the Swedish economic model also diffused some of the pressure on the divide between public and private sector workers. The end of centralized bargaining has made it easier for private sector workers to decouple pay settlements from the public sector.[79] Higher unemployment made the option of cutting the public sector workforce less attractive and shifted attention to transfer programs, where the provision of generous benefits has always depended on keeping the cohort of recipients small. Both the crisis package accepted by the unions and the SAP in late 1992 and the government's 1993 budget were geared toward cuts in transfer programs (sick pay, unemployment insurance, pensions).[80] Thus, while economic problems created added pressure for the welfare state, they did so in a way that encouraged a more dispersed and incremental politics of austerity, rather than a polarization between public and private sector workers.

The government showed little inclination to use the opening for radical restructuring of the welfare state. Coping with the pain of administering austerity weakened the bourgeois coalition's enthusiasm for drastic measures. In any event, only the Conservatives within the governing coalition expressed serious doubts about Sweden's universalist welfare state. Polling data from 1992 indicated overwhelming support for social spending, including increases since 1986 for the major programs.[81] The coalition carefully followed the principal rules of blame avoidance. It sought SAP and union support for crisis packages of reform, purchasing political cover at the price of forgoing opportunities for radical change.[82] A similar approach was taken to pension reform, paralleling the process followed in Germany and the United States. The pension reform introduced in June 1994, based on extensive consultations among the major parties and representative of labor and cap-

[79] Pontusson and Swenson (fn. 19).

[80] Evelyne Huber and John Stephens, "The Swedish Welfare State at the Crossroads," *Current Sweden*, no. 394 (January 1993), 1–7; OECD (fn. 75).

[81] Bo Rothstein, "The Crisis of the Swedish Social Democrats and the Future of the Universal Welfare State," *Governance* 6 (October 1993). Rothstein himself argues that weakening middle-class attachment to the welfare state may have contributed to the SAP's 1991 election defeat, but his article provides no real evidence for this claim and the polling data he presents suggest otherwise.

[82] Huber and Stephens (fn. 80).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ital, seeks to get Sweden's public pension system on a stable, long-term footing without challenging its basic principles.[83]

Far from using its electoral breakthrough and the onset of a budgetary crisis as a golden opportunity to remake the welfare state, Sweden's bourgeois coalition chose a cautious course. Throughout, the coalition studiously avoided initiatives that might lend credence to the accusation that it sought to dismantle the welfare state. The October 1994 elections vindicated the coalition's concerns, but in a way that revealed the unpopularity of even modest assaults on social programs. In the face of Sweden's economic difficulties, the SAP triumphed, posting one of its highest vote totals ever. Moreover, the victory was achieved on a platform that stressed the SAP's intention to reduce the deficit largely through tax increases rather than budget cuts.

## IV. The New Politics of the Welfare State

Economic, political, and social pressures have fostered an image of welfare states under siege. Yet if one turns from abstract discussions of social transformation to an examination of actual policy, it becomes difficult to sustain the proposition that these strains have generated fundamental shifts. This review of four cases does indeed suggest a distinctly new environment, but not one that has provoked anything like a dismantling of the welfare state. Nor is it possible to attribute this to case selection, since the choice of two prototypical cases of neoconservatism (Britain and the United States) and two cases of severe budgetary shocks (Germany and Sweden) gave ample room for various scenarios of radical retrenchment. Even in Thatcher's Britain, where an ideologically committed Conservative Party has controlled one of Europe's most centralized political systems for over a decade, reform has been incremental rather than revolutionary, leaving the British welfare state largely intact. In most other countries the evidence of continuity is even more apparent.[84]

[83] Stephens (fn. 78), 19. Ministry of Health and Social Affairs, *Pension Reform in Sweden: A Short Summary* (Stockholm: Cabinet Office, 1994).

[84] Schwartz (fn. 15) argues that there has been major change in the four small states he studies: Sweden, Denmark, Australia, and New Zealand. His study focuses on the internal organization of public service provision, rather than on the level and quality of services actually provided, and it does not even discuss the transfer payments that account for the majority of welfare-state spending. Even on its own narrow terms, however, Schwartz's study provides remarkably little evidence that the changes he catalogs add up to radical reform rather than the continuous tinkering common in all modern public sectors. The evidence looks credible only for New Zealand, a tiny country on the periphery of the world economy, which clearly faced severe adjustment problems in light of its long (and unusual) tradition of protectionism. It seems far more reasonable to treat this case as an outlier than to view it as the pacesetter in a global march toward radical reform of the welfare state. See Stephens, Huber, and Ray (fn. 38).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

To be sure, there has been change. Many programs have experienced a tightening of eligibility rules or reductions in benefits. On occasion, individual programs (such as public housing in Britain) have undergone more radical reform. In countries where budgetary pressures have been greatest, cuts have been more severe. Over the span of two decades, however, *some* changes in social policy are inevitable; even in the boom years of the 1960s specific social programs sometimes fared poorly. What is striking is how hard it is to find *radical* changes in advanced welfare states. Retrenchment has been pursued cautiously: whenever possible, governments have sought all-party consensus for significant reforms and have chosen to trim existing structures rather than experiment with new programs or pursue privatization.

This finding is striking, given that so many observers have seen the post-1973 period as one of fundamental change in modern political economies. A harsher economic climate has certainly generated demands for spending restraint. Additional pressures have stemmed from the maturation of social programs and adverse demographic trends. Yet compared with the aspirations of many reformers and with the extent of change in fields such as industrial relations policy, macroeconomic policy, or the privatization of public industries, what stands out is the relative stability of the welfare state.

I have suggested that to understand what has been happening requires looking beyond the considerable pressures on the welfare state to consider enduring sources of support. There are powerful political forces that stabilize welfare states and channel change in the direction of incremental modifications of existing policies. The first major protection for social programs stems from the generally conservative characteristics of democratic political institutions. The welfare state now represents the status quo, with all the political advantages that this status confers. Nondecisions generally favor the welfare state. Major policy change usually requires the acquiescence of numerous actors. Where power is shared among different institutions (for example, Germany, the United States), radical reform will be difficult.

As the British and Swedish cases show, radical change is not easy even in a situation of concentrated political power. A second and crucial source of the welfare state's political strength comes from the high electoral costs generally associated with retrenchment initiatives. Despite scholarly speculation about declining popular support for the welfare state, polls show little evidence of such a shift, and actual political struggles over social spending reveal even less. On the contrary, even halting efforts to dismantle the welfare state have usually exacted a high

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

political price. Recipients of social benefits are relatively concentrated and are generally well organized. They are also more likely to punish politicians for cutbacks than taxpayers are to reward them for lower costs. Nowhere is there evidence to support the scenario of a self-reinforcing dynamic, with cutbacks leading to middle-class disenchantment and exit, laying the foundation for more retrenchment. Instead, the recurrent pattern in public-opinion polls has been a mild swing against the welfare state in the wake of poor economic performance and budgetary stress, followed by a resurgence of support at the first whiff of significant cuts.

Nor does the welfare state's political position seem to have been seriously eroded—at least in the medium term—by the decline of its key traditional constituency, organized labor. Only for those benefits where unions are the sole organized constituency, such as unemployment insurance, has labor's declining power presented immediate problems, and even here the impact can be exaggerated.[85] The growth of social spending has reconfigured the terrain of welfare state politics. Maturing social programs produce new organized interests, the consumers and providers of social services, that are usually well placed to defend the welfare state.

The networks associated with mature welfare state programs constitute a barrier to radical change in another sense as well. As recent research on path dependence has demonstrated, once initiated, certain courses of development are hard to reverse.[86] Organizations and individuals adapt to particular arrangements, making commitments that may render the costs of change (even to some potentially more efficient alternative) far higher than the costs of continuity. Existing commitments lock in policymakers. Old-age pension systems provide a good example. Most countries operate pensions on a pay-as-you-go basis: current workers pay "contributions" that finance the previous genera-

[85] Indeed, a cross-national comparison of unemployment programs provides further support for this analysis. The OECD has measured replacement rates for UI (benefits as a percentage of previous income) over time in twenty countries, with data through 1991. This data thus permit, for one program, a recent quantitative appraisal of program *generosity* rather than simply spending levels. In the majority of cases (twelve out of twenty), replacement rates were *higher* in 1991 than the average rate for either the 1970s or the 1980s, while most of the other cases experienced very marginal declines. Organization for Economic Cooperation and Development, *The OECD Jobs Study: Facts, Analysis, Strategies* (Paris: OECD, 1994), chart 16, p. 24.

[86] See Paul David, "Clio and the Economics of QWERTY," *American Economic Review* 75 (May 1985); and W. Brian Arthur, "Competing Technologies, Increasing Returns, and Lock-In by Historical Events," *Economic Journal* 99 (March 1989), 116–31. For good extensions to political processes, see Stephen A. Krasner, "Sovereignty: An Institutional Perspective," in James A. Caporaso, ed., *The Elusive State: International and Comparative Perspectives* (Newbury Park, Calif.: Sage Publications, 1989); and North (fn. 20).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tion's retirement. Once in place, such systems may face incremental cutbacks, but they are notoriously resistant to radical reform.[87] Shifting to private, occupationally based arrangements would place an untenable burden on current workers, requiring them to finance the previous generation's retirement while simultaneously saving for their own.

Over time, all institutions undergo change. This is especially so for very large ones, which cannot be isolated from broad social developments. The welfare state is no exception. But there is little sign that the last two decades have been a transformative period for systems of social provision. As I have argued, expectations for greater change have rested in part on the implicit application of models from the period of welfare state expansion, which can be read to suggest that economic change, the decline in union power, or the presence of a strong state creates the preconditions for radical retrenchment. I find little evidence for these claims.

This preliminary investigation still leaves us some distance from a coherent comparative theory of retrenchment politics. It does, however, suggest some of the building blocks for such a theory. The pressures of a shifting global economy, which have long been at the center of discussions of the contemporary welfare state, continue to deserve major (if more nuanced) attention. What needs more consideration is what happens when these considerable pressures collide with popular, deeply institutionalized public policies. I have emphasized that politicians are likely to pursue strategies that will not damage their chances for reelection. The centrality of electoral considerations, combined with the general unpopularity of welfare state cutbacks, suggests some plausible hypotheses about the political preconditions for significant reform. These hypotheses are only tentative and would need to be subjected to sustained comparative scrutiny. Each, however, is compatible with the analysis of retrenchment outlined here and with the evidence presented.

First, radical retrenchment may be facilitated when there is significant *electoral slack*, that is, when governments believe that they are in a strong enough position to absorb the electoral consequences of unpopular decisions.[88] Thus, one reason for Thatcher's *relative* (though still limited) success may have been the division among her opponents

[87] Thus in Germany, Sweden, and the United States the maturity of existing schemes limited policymakers to very gradual and incremental reforms of earnings-related pension systems. More dramatic reform was possible in Britain because the unfunded earnings-related scheme was far from maturity, having been passed only in 1975. Pierson (fn. 31).

[88] For an example of this argument, see Garrett (fn. 41).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

within a first-past-the-post electoral system. This may have given her more room to pursue unpopular policies that would have been beyond the reach of a government in a precarious electoral position. However, calculating electoral slack *ex ante* is a tricky business, and most governments are likely to proceed cautiously. As I have indicated, even the Thatcher government generally retreated when confronted with widespread opposition.

Second, moments of budgetary crisis may open opportunities for reform. Advocates of retrenchment will try to exploit such moments to present reforms as an effort to save the welfare state rather than destroy it. Framing the issue in this manner may allow governments to avoid widespread blame for program cutbacks. Making the claim of crisis credible, however, generally requires collaboration with the political opposition. In turn, the need for consensus makes it difficult to utilize crises to promote radical restructuring. Thus, while the appearance of fiscal stress encourages downward adjustments in social programs, it is far less clear that it provides a platform for a radical overhaul of social policy.

Third, the success of retrenchment advocates will vary with the chances for lowering the visibility of reforms. Those seeking retrenchment will try to avoid political outcries by diminishing the visibility of their cutbacks or by trying to hide their own responsibility for unpopular outcomes. Success in these efforts, I have argued, depends partly on the design of political institutions. Whether political authority is concentrated or not helps to structure the choices available to retrenchment advocates. Where authority is concentrated (as in Britain and Sweden), governments will be hard-pressed to avoid blame for unpopular decisions, but they will have a greater capacity to develop and implement strategies that obscure cutbacks. Governments in more fragmented systems must fashion strategies that minimize the need to force multiple policy changes through institutional veto points. However, they may find it easier to duck accountability for unpopular policies. Federalism, for example, opened up considerable possibilities for Reagan to shift the blame for cuts in some programs, a tactic that is central to the current efforts of congressional Republicans.

Finally, the prospects for changing institutions (the rules of the game) may be of great significance. If retrenchment advocates can restructure the ways in which trade-offs between taxes, spending, and deficits are presented, evaluated, and decided, they may be able to shift the balance of political power. So far, these institutional shifts have been rare, but several instances may be of growing relevance. In Europe

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

the increasing policy significance of the EC may alter the terrain for struggles over the welfare state. If reforms can be presented as legally required or economically imperative because of the single market or moves toward monetary union, national governments may be freed from some blame for welfare-state cutbacks.[89] In the United States the new Republican majority in Congress deferred efforts to cut programs until after a strong (but only modestly successful) push to change the rules of the game. The intent of the rule changes was to increase the salience of taxes and create a more favorable climate for attacking social spending.

If this analysis suggests some plausible sources of cross-national variation, it also highlights the need to disaggregate welfare states and consider variations across programs. Indeed, in the four cases considered outcomes often differed more across programs (for example, the contrast between council housing and the NHS in Britain) than across countries. It is commonly argued that the crucial distinction across programs will be between universal programs and those that target the poor, and that the latter will be especially vulnerable.[90] Yet the current investigation does not support this assertion. Rather, variations in outcomes across programs in the four countries do not generally track the universal/targeted divide. Among the likely reasons that targeted programs have generally not proved more vulnerable: cuts in these programs tend to yield only minimal budgetary savings, and conservative governments interested in radical reform object the most to the universal programs that require high tax rates and compete with plausible private alternatives. Instead, the current investigation suggests that a promising area of research concerns the features of programs that allow governments either to obscure the *impact* of retrenchment on voters or to diminish their own *accountability* for unpopular reforms.[91] Programs that are poorly indexed, for example, make it easier to pursue a low-visibility strategy of allowing inflation to gradually erode the value of benefits.

All of these hypotheses build on the core argument of this essay: that frontal assaults on the welfare state carry tremendous electoral risks.

[89] For an argument about how EC institutions may allow blame-avoiding behavior on the part of member state governments, see Andrew Moravcsik, "Why the EC Strengthens the State" (Manuscript, 1994).

[90] Robert Kuttner has called this "the most fundamental principle in the political economy of social spending." Kuttner, "Reaganism, Liberalism, and the Democrats," in Sidney Blumenthal and Thomas Byrne Edsall, eds., *The Reagan Legacy* (New York: Pantheon, 1988), 113. For a critique, see Pierson (fn. 12), 6, 170.

[91] See Pierson (fn. 12), 17–26, 169–75.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

The contemporary politics of the welfare state is the politics of blame avoidance. Governments confronting the electoral imperatives of modern democracy will undertake retrenchment only when they discover ways to minimize the political costs involved. But as I emphasize, such techniques are hard to come by. While this analysis suggests some of the possible keys to variation in policy outcomes, the most significant finding concerns not variation but commonality. Everywhere, retrenchment is a difficult undertaking. The welfare state remains the most resilient aspect of the postwar political economy.

Understanding why this is so requires that old arguments be rethought and recast to address the exigencies of a new setting. At a time when historical institutionalism has become fashionable, this conclusion has broad implications for the study of comparative politics. The strong calls to incorporate historical analysis into the study of contemporary politics are compelling.[92] Yet we must remain cognizant of the hazards of drawing on history in the wrong way. There are significant dangers in using historical *analogies* to study contemporary social politics, since the goals of social policy reformers and the context in which they operate have undergone profound change. Instead, historically grounded analysis should emphasize that social policy change is a process that *unfolds over time*. My focus on the impact of inherited social policy structures draws on this precise point. The growth of the welfare state has transformed the politics of social policy. A historical perspective should stress that today's policymakers operate in an environment fundamentally shaped by policies inherited from the past, rather than suggesting that current politics will echo the conflicts of a previous era.

[92] Sven Steinmo, Kathleen Thelen, and Frank Longstreth, eds., *Structuring Politics: Historical Institutionalism in Comparative Analysis* (Cambridge: Cambridge University Press, 1992).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# RACE-MAKING AND THE NATION-STATE

By ANTHONY W. MARX*

W. E. B. Du Bois described "the problem of the color line" as a central concern of this century, and indeed in the United States and South Africa the era has seen the elaboration of postslavery segregation and protest. These experiences have confounded the expectations of Marxists and modernization theorists alike that racial identification and mobilization were merely archaic residues and would disappear. If anything, industrialization, class conflict, and rising nationalism have reinforced racial domination and conflict.[1] Although these processes appear to be interconnected, the situations that have shaped racial discourse and practice, produced legally encoded racial identity, and provoked conflict remain to be fully specified. The end of the century may be a particularly opportune time for such an assessment.

Any analysis of racial ideology, domination, and conflict must begin with the prior question of why race becomes salient at all—it is not sufficient to argue that certain social factors polarize race relations, for this assumes race as a preexisting category. Thus, although racism and images of primordial difference do seem to be pervasive where peoples of varying ancestry come into contact, this similarity does not account for the different ways in which race has been constructed. Race is not found, but "made" and used. Therefore, we must shift from describing race "as a tool of analysis" to considering it "as the object of analysis."[2]

* I am grateful for the comments and suggestions provided by Karen Barkey, Douglas Chalmers, Stephen Ellman, Eric Foner, Charles V. Hamilton, Carlos Hasenbalg, Jennifer Hochschild, Tom Karis, Ira Katznelson, Mark Kesselman, David Laitin, Manning Marable, T. Dunbar Moodie, Mark Orkin, Lloyd Rudolph, Jack Snyder, Steven L. Solnick, Sidney Tarrow, Rupert Taylor, Charles Tilly, Harrison White, and the Identities workshop of Columbia's Center for Social Sciences. Support has generously been provided by the United States Institute of Peace, the Social Sciences Research Council, the Tinker Foundation Fellowship of the Institute for Latin American and Iberian Studies at Columbia University, the Center for Afro-Asian Studies in Rio de Janeiro, and the Harry Frank Guggenheim Foundation.

[1] See Robert Miles, *Racism* (London: Routledge, 1989); Michael Omi and Howard Winant, *Racial Formation in the United States* (New York: Routledge and Kegan Paul, 1989); John Rex, *Race Relations in Sociological Theory* (London: Routledge, 1970); William Julius Wilson, *Power, Racism and Privilege* (New York: Free Press, 1973).

[2] Rupert Taylor, "Racial Terminology and the Question of 'Race' in South Africa" (Manuscript, 1994).

*World Politics* 48 (January 1996), 180–208

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Why and how do social distinctions and conflict come to be projected in terms of physical differences of color or purported race in the first place? More precisely, why were blacks in particular so categorized and subjected to race-specified domination, provoking conflict, or not?

I propose to examine the causes and consequences of official "race-making" by means of a comparative analysis of South Africa, the United States, and Brazil, the most prominent cases in which European settlers dominated indigenous and slave populations of African origin.[3] In each of these major regional powers, social and economic measures indicate significant and persistent disparities between black and white that built on the legacy of slavery. But the different contexts set them apart and therefore make them useful for a comparative study of the dynamics of official racial domination. Dutch, British, and Portuguese settlers brought varying practices, religions, and traditions to their colonies, making for economic development and state consolidation that followed divergent paths. Unlike in South Africa, the United States promised equal rights in its Constitution, to which African Americans could and did appeal. Demographics also differed: those of African descent are a minority in the U.S., indigenous Africans constitute the majority in South Africa, and those of African and European ancestry are roughly equal in number in Brazil.

While racial discrimination was pervasive in the early history of South Africa, the United States, and Brazil, postabolition state policies encoded very different racial orders. All three cases faced extended "moments" of relative indeterminacy and an unhappy repertoire of possible racial configurations in the aftermath of slavery, at the time of emerging state consolidation. In both South Africa and the United States the result—with significant differences—was official racial ideology, imposed categories of segregation and conflict, and only recent dismantling of legal discrimination. In contrast, postabolition Brazil avoided legal distinctions based on race and instead projected an image of "racial democracy." Despite the commonality of early racism and continued inequality, Brazil did not enact anything equivalent to apartheid or Jim Crow. These alternative outcomes pose a useful puzzle for comparative analysis.

I begin by assessing earlier explanations of race-making as being

[3] For other comparative studies of these cases, see Pierre Van den Berghe, *Race and Racism* (New York: John Wiley and Sons, 1967); Stanley B. Greenberg, *Race and State in Capitalist Development* (Johannesburg: Ravan, 1980); George M. Fredrickson, *White Supremacy* (New York: Oxford University Press, 1981); John W. Cell, *The Highest Stage of White Supremacy* (Cambridge: Cambridge University Press, 1982); Carl N. Degler, *Neither Black nor White* (New York: Macmillan, 1971).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

based on differences of slavery, culture, colonial rule, miscegenation, and economic development. While such influences must be incorporated into the present analysis, I dispute the argument that these legacies and interests preordained a more tolerant racial order in Brazil. Brazilians may have retrospectively interpreted their past to reinforce an image of racial tolerance, but in fact racism was as evident early on in Brazil as it was in the United States or South Africa (though it differed in form), and the inequality in Brazil continued. By contrast, in the United States and South Africa past discrimination was embraced and used to justify segregation and exclusion. This difference in kind is not explained by comparable degrees of discrimination or exploitation.

The official projects of Jim Crow in the United States and apartheid in South Africa were shaped by distinct paths and challenges to building the nation-state. Disputes over the treatment of blacks and slaves had contributed to tensions among whites that culminated in the Civil War and the Boer War, respectively. Consolidated by these conflicts and their commitment to labor coercion, Southerners and Afrikaners had proved themselves a threat that had to be reckoned with if stability and development were to be restored. Blacks had not proved comparably disruptive, had already been distinguished by earlier racism, and could be excluded to appease Southern and Afrikaner demands. Agreement on a racially defined "other" as a common enemy defined and encouraged white unity. Thus, the same issue of race that had exacerbated prior conflict was used to heal it, as racial domination gradually transformed a potential triadic conflict among white factions and blacks into a more manageable dyadic form of "white over black." Such strategic adjustment can be described schematically as bolstering unity. But policy that appears functional in retrospect actually emerged from ongoing conflict, competition, and maneuvering of actors seeking solutions to real problems. Although intrawhite tension remained, it was contained within a unified polity. Racial domination was repeatedly reinforced to consolidate the nation-state.

Brazil provides an essential comparison, for there no equally violent ethnic or regional conflict impeded nation-state consolidation. Unity did not require a racial crutch of formal discrimination; rather, "racial democracy" emerged there as an ideological project of a state anxious to unify popular support without formal exclusion. As a result, explicit categories of racial domination were not officially constructed and images of past tolerance were encouraged.

I will conclude by discussing how state policies provoked and shaped black protest, eventually forcing the abandonment of official discrimi-

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

nation where it had been enacted. In South Africa and the United States racial domination unifying whites proved double-edged, having the unintended consequence of inciting black protest. Efforts to resolve one conflict exacerbated another. Apartheid and Jim Crow were then ended, as black protest replaced intrawhite conflict as the most pressing threat to the nation-state. In Brazil, with no clear target of state ideology and segregation policy to organize against—no apartheid or Jim Crow to challenge or reform—little Afro-Brazilian protest emerged, and racial conflict was largely avoided despite considerable socioeconomic inequality.

## Historical and Cultural Explanations of Race

The lack of explicit racial categorization, domination, and conflict in postabolition Brazil has been explained as the result of racial tolerance imported by Portuguese colonialists. The imposition of racial domination and conflict in the United States and South Africa would then be explained by the extent to which the British and Dutch had a contrary set of influences. To assess this argument about colonial influences, one must look to the historical record. Did the Portuguese in fact import racial tolerance to Brazil, or is this claim an instance of ex post interpretation?

In Brazil, the U.S., and South Africa slavery begun under colonialism established the fundamental pattern of race relations. Gilberto Freyre in the 1930s and other analysts have suggested that slavery in Brazil was relatively benign, a tradition they contend was carried over into more tolerant postabolition race relations. According to the "Tannenbaum thesis," Brazilian slavery was notable for its recognition of the slaves' humanity: they were allowed to marry, own property, and even buy their own freedom.[4] Contrary to this argument, however, was the fact that Brazilian slavery was particularly brutal. Slaves were guaranteed the right to buy their own freedom only after 1871 (and even then the practice was difficult), marriage among slaves was rare, property held by slaves was in constant jeopardy, and manumission of less productive slaves meant that the elderly and sick were abandoned to their fate after years of work.[5] Compared with other slave powers, Brazil remained longer and more fully dependent on continued importation of new slaves because the harsh conditions under which slaves lived did not allow for reproduction of their numbers. Mortality among slave

[4] Frank Tannenbaum, *Slave and Citizen* (New York: Knopf, 1946). See van den Berghe (fn. 3), 67.
[5] Degler (fn. 3), chap. 2.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

children was estimated to be 80 percent, with slaves working in the mines generally surviving for only seven to ten years.[6] Having no free region to which they could flee, Brazilian slaves revolted in dramatic numbers.[7]

Tannenbaum's thesis rests on an overly generous interpretation of the real conditions of Brazilian slavery. It is true that the Portuguese did establish a somewhat less strict divide between slave and free than was enforced in the U.S., but they also established a particularly deadly form of bondage. The image of a Brazilian "benign master" was a myth. Tannenbaum also ignored the comparable imagery of paternalism toward slaves in the Southern United States.[8] Such paternalism did not preclude postabolition racial domination in the U.S., as it purportedly did in Brazil. Nor did early abolition in South Africa preclude segregation and exclusion. Though slavery took different forms in Brazil, the U.S., and South Africa, in all three it fostered attitudes of a primordial black inferiority and established patterns of domination and inequality. This similarity cannot account for the difference in postabolition racial orders.

A specific feature of the argument about Brazilian slavery concerns the influence of Catholicism. Tannenbaum argues that "the Catholic doctrine of the equality of all men in the sight of God" produced better treatment of slaves and generally greater racial tolerance than did the more exclusive Dutch or British Protestantism.[9] The hierarchy of the Catholic church also purportedly militated against an exclusively biracial divide. Of course, when one considers the history of the Crusades, the Inquisition, and the rapacious colonialism pursued by the Spanish and Portuguese with the support of the church, it is difficult to avoid skepticism about official Catholic tolerance. The church also enacted its own internal policies of racial discrimination in Brazil. Furthermore, as the Catholic church in Brazil was not strong enough to force abolition, it "could never live up to its early promise as a force against the slave regime."[10] That Catholicism projected a more inclusive or toler-

[6] Robert Conrad, "Nineteenth Century Brazilian Slavery," in Robert Brent Toplin, ed., *Slavery and Race Relations in Latin America* (Westport, Conn.: Greenwood Press, 1974), 150; Clóvis Moura, *História do Negro Brasileiro* (São Paulo: Ed Atica, 1989), 14.

[7] Moura (fn. 6), 15–32.

[8] See Eugene D. Genovese, *Roll, Jordan, Roll: The World the Slaves Made* (New York: Random House, 1972).

[9] Tannenbaum (fn. 4), 53. The same argument is put forward in Louis Hartz, *The Founding of New Societies* (New York: Harcourt, 1964), 152. For a discussion of the role of Calvinism in the emergence of racial discrimination in South Africa, see Jonathan N. Gerstner, *The Thousand Generation Covenant* (Leiden: E. J. Brill, 1991).

[10] Genovese (fn. 8), 177; Caio Prado, Jr., *The Colonial Background of Modern Brazil* (Berkeley: University of California Press, 1969), 327; Winthrop D. Jordan, *White over Black* (New York: W. W. Norton, 1968), 206.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ant image is therefore more a reflection of retrospective interpretation than of historical reality.

Colonialism in Brazil was most distinguished by the direct role of the Portuguese state. Whereas the Dutch and the British relied on private companies to develop their colonies, the Portuguese crown invested on its own behalf.[11] Portuguese colonialism developed early, before a strong private sector had emerged in the home country. Indeed, Portugal's own economic development consistently lagged behind that of the Dutch and the British, so there was never an equally strong private sector. The Portuguese crown had little choice but to use its own resources, establishing a pattern of strong state consolidation and centralized power.

Did the greater degree of direct, centralized state involvement in Portuguese colonialism produce early racial tolerance? The historical record suggests not. It was after all the Portuguese state that engaged in one of the greatest slave trades in history. The early abolition of slavery within Portugal in 1773 explicitly did not preclude the much more pervasive, stubbornly maintained slavery in its colonies. The slave trade to Brazil was ended only under pressure from Britain, leading to gradual but late abolition. The Portuguese state enacted its own "color bar" at home and abroad, with the result that there were relatively few "darker-skinned" state officials.[12] Portuguese colonialism in Africa was similarly discriminatory: with its use of forced labor, it produced "the absolute literal nadir of African misery."[13] Perry Anderson concludes that "the falsity of Portuguese claims of special tolerance is evident," with the myth of such tolerance having been deliberately projected to obscure "economic and social retardation."[14] The Portuguese colonial state was stronger than its private sector, and it used that strength to project an exaggerated image of tolerance.

The absence of official racial domination in postabolition Brazil has been explained as the result of Portuguese colonial policies—"humanitarian" slavery—or of Catholicism. But Portuguese colonialism and Brazilian slavery were vicious, the early Brazilian state was not color blind, and the Catholic church was at best ambivalent toward blacks and certainly unable to force better treatment of them. Brazil's early

[11] Perry Anderson, "Portugal and the End of Ultra-Colonialism 2," *New Left Review* 16 (July–August 1962).

[12] C. R. Boxer, *Four Centuries of Portuguese Expansion, 1415–1825* (Berkeley: University of California Press, 1969), 42.

[13] Anderson (fn. 11), 93. See also Gerald J. Bender, *Angola under the Portuguese: The Myth and the Reality* (Berkeley: University of California Press, 1978).

[14] Anderson (fn. 11), 110, 113.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

racism was distinctive but still comparable to that of the U.S. and South Africa. The latter two justified their explicit racial domination on the basis of early beliefs and patterns of slavery and discrimination. After abolition Brazilians abandoned the official discourse of racism, and embraced historical interpretations consistent with "racial democracy." The historical legacy of inequality in Brazil was merely camouflaged, and quiescence among Afro-Brazilians thereby encouraged. Earlier racism was not wiped away, for as Edward Said has suggested in another context, images of inferiority and the reality of inequality remained beneficial to whites.[15] But unlike elsewhere the past was reconceived into a benign image, one that did not reflect historical fact. Instead, varying interpretations and outcomes were shaped by subsequent processes building upon the past, in a conjunctural process.

## The Miscegenation Argument

Carl Degler provides one of the most widely held explanations of differences in how race has been socially constructed. He argues that Brazil could not develop a biracial ideology or formalize rigid racial classification and domination because of the high level of mixing between races. Miscegenation had purportedly also provided for greater social fluidity in Brazil, with people of mixed race able to move up to a higher socioeconomic status via a "mulatto escape hatch." As a result, race relations were less polarized and conflictual than in the U.S., or for that matter than in South Africa. In those cases, more stark physical differences supposedly provided the basis for official race categories reinforcing socioeconomic discrimination.

The strength of Degler's argument rests on the historical fact of significant miscegenation in Brazil. Portuguese colonialists came to Brazil for trade more than to settle, particularly as compared with the Dutch and British who came to the U.S. and South Africa. And as compared with the other two cases, Portuguese colonialists included few women.[16] As a result, Portuguese men engaged in significantly higher levels of miscegenation. Social mores and sexual tastes and practices developed accordingly, producing a population that remains notable for its continuum of physical variation. By 1872 the Brazilian census registered 42 percent of the population as mulatto, with this group

[15] Said, *Orientalism* (New York: Random House, 1978).

[16] Prado (fn. 10), 119; E. Bradford Burns, *A History of Brazil* (New York: Columbia University Press, 1970), 37.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

relied on to serve intermediary functions of control over "darker" slaves.[17]

Although miscegenation in Brazil is a historical fact, Degler's critics have disputed his interpretation of this fact. Even during slavery, mulattoes remained subject to reenslavement and discrimination.[18] With a few notable exceptions, mulattoes were and remain largely underprivileged. Either the escape hatch has closed or it never existed. Indeed, Degler himself did not provide any statistical evidence of black mobility, beyond simply demonstrating the level of miscegenation. Recent scholarship has established that the difference in socioeconomic status between mulattoes and blacks is insignificant in comparison with the relative privilege of whites. "The average income for whites was found to be about twice that for nonwhites both in 1960 and in 1976."[19]

Brazil constructed an informal racial order that was highly discriminatory against "blacks and browns," such that earlier patterns of inequality were maintained. Only a few mulattoes advanced—enough to encourage belief in mobility. Thus, continued popular belief in the mulatto escape hatch appears to be based less on material conditions than on an ideological project encouraging assimilation. Miscegenation in itself did not produce the myth of mobility, but this image did dilute potential conflict.

In the United States and South Africa, people of "mixed race" were classified according to varying categories and policies. Miscegenation never approached the levels of Brazil; indeed it remained illegal in the United States and South Africa until recently. Nevertheless, miscegenation did occur in large numbers, with varying outcomes. In the United States, 13 percent of blacks in 1860 were categorized as mulatto, rising to 21 percent by 1920. This category eventually disappeared with the refinement of the "one drop of blood" rule, with whites confident that they could impose biracial domination over a "black-brown" minority.[20] Recent scholarship has demonstrated that the majority of

[17] Charles H. Wood and J. A. Magno de Carvalho, *The Demography of Inequality in Brazil* (Cambridge: Cambridge University Press, 1988), 141; Marvin Harris, *Patterns of Race in the Americas* (New York: Walker, 1964).

[18] Robert Conrad, *The Destruction of Brazilian Slavery* (Berkeley: University of California Press, 1972), 12; Thomas E. Skidmore, "Bi-Racial U.S. versus Multi-Racial Brazil: Is the Contrast Still Valid?" (Manuscript, June 1992), 15.

[19] Nelson do Valle Silva, "Updating the Cost of Not Being White in Brazil," in Pierre-Michel Fontaine, ed., *Race, Class, and Power in Brazil* (Los Angeles: Center for Afro-American Studies, University of California, 1985), 54. See also Nelson do Valle Silva and Carlos A. Hasenbalg, *Relações Raciais no Brasil Contemporâneo* (Rio de Janeiro: Rio Fundo, 1992).

[20] Genovese (fn. 8), 414; Fredrickson (fn. 3), 134; F. James Davis, *Who Is Black? One Nation's Definition* (University Park: Pennsylvania State University Press, 1991), 40; Abdias do Nascimento, *Brazil: Mixture or Massacre?* (Dover: Majority Press, 1979), 65.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

African Americans have a significant proportion of white ancestry, with those having "lighter" skin marginally better off economically.[21] In South Africa a "colored" population of more than three million attests to significant miscegenation and immigration.[22] Explicit rules were required to demarcate coloreds, who did enjoy some greater privilege than Africans, thereby diluting the "black threat" to the white minority. Such privilege was eroded as white power was consolidated.

Miscegenation was celebrated and mulattoes assimilated in Brazil, but this pattern was not followed in the other two cases. In the U.S. and South Africa, mobility was officially blocked, provoking "nonwhite" unity and resistance. According to Degler, miscegenation in itself diminishes the possibility of such strict racial domination, discrimination, and resulting conflict. Instead, South African and U.S. authorities resolved physical ambiguities by drawing strict racial boundaries, limiting mobility, and stirring up antagonism. Substantial miscegenation did not preclude the development of apartheid or Jim Crow as it purportedly did in Brazil. Even the white South African minority eventually alienated its potential colored allies.

Though people often believe and act as if race is physically determined, shifts of beliefs, categories, and practices demonstrate the contrary. No doubt, Brazil's higher level of miscegenation would have made it more difficult to impose strict categories of domination over mulattoes. Without such a demarcation conflict was less likely. But the U.S. and South Africa did impose such categories on their mixed populations, and conflict was accordingly provoked. Physical differences, mixing, and demographic proportions were significant but did not preordain specific racial categorization, domination, and conflict, or lack thereof. To explain these divergent outcomes requires looking beyond the biological fact of miscegenation, to why continuous physical variation was interpreted as such or forced into strict categories of race.

## Economic Explanations of Race

Race-making cannot be disentangled from the process of economic development. Industrialization, coming in tandem with increased immigration and urbanization, also coincided with the rise of formal segregation in the U.S. and South Africa. The development of Jim

[21] Verna M. Keith and Cedric Herring, "Skin Tone and Stratification in the Black Community," *American Journal of Sociology* 97 (November 1991).

[22] Central Statistical Services, *South African Statistics, 1988* (Pretoria: Government Printer, 1988), tables 1.7, 7.7.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Crow and apartheid has been described as an effort to protect whites from black competition. Lesser economic development and competition would then account for Brazil's lack of similar policies.[23] More specific economic explanations have suggested that racial categorization and segregation served the interests of capital in providing for cheap black labor, or served the interests of privileged white labor by reserving better jobs and ensuring higher wages.[24] The implication is that state policies regarding race were not autonomous but were determined by particular class interests.[25] Comparative analysis of the U.S., South Africa, and Brazil allows for an assessment of these arguments.

In South Africa segregation and apartheid fed the process of economic development and proved highly profitable. British capital first provoked the Boer War in order to gain control over the country's riches and then encouraged state policies of racial domination to ensure a supply of cheap black labor in the mines.[26] But persistent segregation cannot be attributed to varying and divided business pressure. Beginning with the fall of gold prices in the early 1920s, mining capital was eager to relax segregation in order to displace more expensive white labor. By the 1970s manufacturing capital advocated the end of apartheid in order to ensure more skilled black labor and an expanded market among blacks.[27] But capital's pressures for reform were rebuffed by the state, which acted to protect the interests of white, largely Afrikaner labor. Indeed, after the 1922 Rand Revolt of emerging Afrikaner capital and of Afrikaner miners protesting business efforts to replace them with lower-paid blacks, Hertzog's new government reinforced the color bar preferential to white workers.[28] The National Party government in power after 1948 remained dedicated to such protection of Afrikaner workers as the majority of the electorate. Fearing a repeat of the Rand Revolt by white workers protecting their privilege, capital acquiesced, appeased by continued profits.[29]

Neither the interests of South African capital nor general economic

[23] See van den Berghe (fn. 3), 27–30; Cell (fn. 3), 104; Susan Olzak, *The Dynamics of Ethnic Competition and Conflict* (Stanford, Calif: Stanford University Press, 1992).

[24] Edna Bonacich, "A Theory of Ethnic Antagonism: The Split Labor Market," *American Sociological Review* 37 (October 1972).

[25] Michael Burawoy, "The Capitalist State in South Africa," in Maurice Zeitlin, ed., *Political Power and Social Theory* (Greenwich, Conn.: JAI Press, 1981), 2:282.

[26] Cell (fn. 3), 62–67; Harold Wolpe, "Capitalism and Cheap Labor Power in South Africa," *Economy and Society* 1, no. 4 (1972).

[27] Deborah Posel, *The Making of Apartheid* (Oxford: Clarendon, 1991).

[28] Fredrick A. Johnstone, *Class, Race and Gold* (London: Routledge, 1976).

[29] Francis Wilson, *Labour in the South African Gold Mines, 1911–1969* (Cambridge: Cambridge University Press, 1972), 11; Greenberg (fn. 3), 129, 151.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

rationality were as determinant as the interests of white labor. The South African state reinforced segregation while still under formal British rule and despite later business pressure for reform. After 1948 the state pursued apartheid despite the tremendous cost of regulation and the manifold inefficiencies. Throughout, white workers' demands for privilege were met. To keep development going, however, the interests of white labor had to be balanced against the demands of capital, efficiency, and black labor. Various "reforms" were implemented over the objections of white labor, for instance, with cheaper black labor gradually filling more jobs and with black unions legalized in the late 1970s.[30]

The overriding conclusion is that "the principle function of segregationist ideology was to soften class and ethnic antagonism among whites, subordinating internal conflicts to the unifying conception of race."[31] Class antagonism did reinforce the conflict between English capital and Afrikaner workers. But the state was not in the exclusive service of either side of this overlapping class and ethnic conflict in which it was embedded. Instead, the state imposed varying forms of racial domination to unify whites and to diminish conflict, compromising between conflicting interests. Stability was thus encouraged, and economic development proceeded, providing revenues to the state.

In the United States "the golden age of racism" paved the way for industrial expansion.[32] Capital benefited from segregation, employing cheap black labor to increase profits and to break strikes by white workers. But profit alone cannot explain why Jim Crow was elaborated before the greatest spurt of industrialization and in the less industrialized South.[33] Apparently segregation more directly served the interests of white labor, especially where blacks were more numerous. Yet many Southern white workers understood that their interests might be better served by working-class unity across race lines, as advocated by the Populist movement.[34] This movement was defeated by white planters' racism, embraced by workers. Poor whites, including immigrants in the North, were "prepared to pay the price of their own distress in order to keep the Negro still lower."[35] Labor's narrowly defined interests were not consistently served by segregation, but the relative social status of its white members was bolstered.

The American racial order appeased white workers and Southerners,

[30] David Yudelman, *The Emergence of Modern South Africa* (Westport, Conn.: Greenwood Press, 1983).
[31] Cell (fn. 3), 234.
[32] Wilson (fn. 1), 56.
[33] Fredrickson (fn. 3), 215–16.
[34] Olzak (fn. 23), 110–11; David R. Roediger, *The Wages of Whiteness* (London: Verso, 1991).
[35] Gunnar Myrdal, *Am American Dilemma* (New York: Harper and Row, 1944), 457.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

while also meeting the general interests of Northern capital in maintaining order. "Disorder and violence destroys business altogether,"[36] after all, and Jim Crow helped to contain such conflict. Racial domination encouraged cross-class white unity, rather than exclusive loyalty to one's own class interests. Intrawhite conflict was diminished, and growth proceeded.

Brazil appears to confirm the more general pattern of economic explanations. A lower level of economic development and competition coincided with the absence of apartheid or Jim Crow.[37] But if "racial democracy" reflected the early lack of economic development, then rising industrialization should have produced more explicit patterns of racial domination, at least in the more developed Southeast and during times of economic boom.[38] But that did not happen.

Rather, the interests of white workers and capital were both advanced under Brazil's "racial democracy." The relative privilege of white workers has been maintained by higher wages without an official racial order and segregation. For instance, in 1960, in the relatively developed area of Rio de Janeiro, the average monthly income of blacks was Cr $5,440; for mulattoes it was Cr $6,492; and it was almost double that, Cr $11,601, for whites.[39] Once the pattern of inequality had been established, such privilege did not require explicit racial domination to sustain itself. Business also profited from cheap black labor. Moreover, absent official segregation poor blacks could believe that advancement was possible. The image of racial tolerance thus encouraged cross-class unity, stability, and growth, in this instance, by avoiding explicit racial domination and conflict altogether.

The racial order in each of the three cases certainly reflected and enhanced economic development, but in complex ways. Apartheid and Jim Crow diluted intrawhite competition that threatened stability and growth, yet growth and competition did not lead to such policies in Brazil. In South Africa capital's interests were not unified or consistently served. Business was forced to comply with apartheid as the demands of white labor for racial preferences were more consistently met. But resulting working-class division by race was economically disad-

[36] Joel Williamson, *A Rage for Order* (New York: Oxford University Press, 1986), 250. See also Karl Polanyi, *The Great Transformation* (Boston: Beacon, 1994), chap. 1.

[37] Emilia Viotti da Costa, *The Brazilian Empire* (Chicago: University of Chicago Press, 1985), 55; Cell (fn. 3), 11; Harris (fn. 17), 96–98.

[38] Degler (fn. 3), 99; Carlos Hasenbalg, "Race Relations in Post-Abolition Brazil" (Ph.D. diss., University of California, Berkeley, 1978), x, 240.

[39] Nelson do Valle Silva, "Black-White Income Differentials: Brazil, 1960" (Ph.D. diss., University of Michigan, 1978), 99.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

vantageous to labor, for instance, when blacks were used to displace whites or to break strikes. By the 1930s many American trade unionists advocated cross-race working-class unity and organization, which employers resisted.[40]

Since capital and white workers often had contrary interests, both could not be served exclusively. In South Africa and the U.S. varying state policies sought to reconcile conflicting interests among whites by unifying them as a race. If racial domination served to unify whites across class lines, then narrow class interests by themselves cannot explain this outcome. Nor can class assertions in Brazil by themselves account for "racial democracy," which also appeased such interests. Brazilian capital profited from low black wages, higher wages for whites were maintained, and the prospect of black mobility was exaggerated.

In all three cases, real or potential class conflict had to be resolved to ensure stability—the most fundamental requirement for both economic development and consolidation of the nation-state. Class interests had exacerbated the ethnic division in South Africa and the regional tension in the U.S., and they posed a potential threat to national unity in Brazil. In all three cases, states were not simply captive of one interest, but instead acted with relative autonomy to contain and respond to conflicting interests. To explain how conflict was so diminished or avoided within distinctive racial orders requires analysis of the political dynamics.

## Race-Making and the Nation-State

The construction of racial domination requires clearly established boundaries of physically distinct categories. History, physical differences, and economic development may reinforce such categorical domination, but they do not preordain it or the form it will take. It is state policy that officially categorizes people as black, white, or mulatto and that enforces legal discrimination. As Justice John Marshall Harlan asked rhetorically in 1896, "What can more certainly arouse race hate, what more certainly create and perpetuate a feeling of distrust between these races, than state enactments[?]"[41] Indeed, recent scholarship has pointed to the state as the central actor in race-making.[42] Of course, ar-

[40] Philip S. Foner, *Organized Labor and the Black Worker, 1619–1973* (New York: Praeger, 1974), chaps. 14–16.

[41] As quoted in Burke Marshall, *Federalism and Civil Rights* (New York: Columbia University Press, 1964), 85.

[42] I am here applying arguments about ethnicity to the more specific case of race. See, for example, Crawford Young, *The Politics of Cultural Pluralism* (Madison: University of Wisconsin Press, 1976); Cynthia Enloe, "The Growth of the State and Ethnic Mobilization: The American Experience,"

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

guing that it is the state which defines and enforces racial boundaries does not explain why the state should or should not do so. The state may have the capability of "making" races, but it remains to specify the situation that may or may not lead the state to exercise its power in this way.

In all three of the cases examined here, the state faced an extended historical moment during which modern race relations were configured, with divergent outcomes. For the United States and Brazil that moment came with the abolition of slavery. Earlier racial discrimination was formally reinforced in the U.S. and not so enacted in Brazil. Slavery (or abolition of it) cannot in itself explain these divergent outcomes. For South Africa, where slavery was abolished earlier amid continued discrimination, the comparable moment came when the country was unified for the first time and national race policies were enacted. In all three cases the consolidation of a postabolition or united state raised the dilemma of whether and how to incorporate those of African descent. This dilemma had to be addressed to avoid or at least diminish conflict that could divide the nation and thereby disrupt central rule and development. Policies evident in transitional moments were then later refined.

The history of South African racial domination began with the first arrival of whites on the Cape in the seventeenth century. Religion was used to justify discrimination against "heathens." However, most historians agree that explicit and formalized racial discrimination was elaborated two centuries later, forged by the conflict between two European "fragments."[43] After their victory in the Napoleonic Wars, the British took control of the Cape Colony from the descendants of the Dutch, the Afrikaners. The British enforced early abolition and more liberal racial policies of selective discrimination.[44] Citing their "determination . . . [to] preserve proper relations between master and servant,"[45] thousands of Afrikaners trekked north to escape British rule, establishing their own republics during the 1850s, reinforcing racial domination and labor coercion. No single policy toward the natives could emerge under such circumstances, although discrimination was prevalent.

The uneasy stasis of a divided country was soon disrupted. Britain's

*Ethnic and Racial Studies* 4 (April 1981), 123–36; Joanne Nagel, "The Political Construction of Ethnicity," in Susan Olzak and Joanne Nagel, eds., *Competitive Ethnic Relations* (Orlando, Fla.: Academic Press, 1986).

[43] Hartz (fn. 9), 3.

[44] Thomas Karis, "South Africa," in Gwendolen Carter, ed., *Five African States* (Ithaca, N.Y.: Cornell University Press, 1963), 480–81.

[45] W. A. de Klerk, *Puritans in Africa: A History of Afrikanerdom* (Middlesex, England: Penguin, 1975), 23. De Klerk is here quoting Piet Retief, from 1837.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

aspirations expanded, fed by the discoveries in the north of diamonds in 1877 and of gold in 1886, and by resulting pressures for a unified railroad system.[46] The ensuing conflict between the British and Afrikaners came to a head at the turn of the century, with the costly British victory in the Boer War. This conflict solidified distinct English and Afrikaner group solidarity, both of which had been riven by internal divisions. In the war's aftermath exacerbated Afrikaner-English animosity threatened to undermine British efforts to shape a militarily and economically coherent united South African polity.[47]

The British impetus to reconcile with the Afrikaners after the Boer War set the terms for the segregation of blacks that was to become central to South African state making. As the British high commissioner, Sir Alfred Milner, argued as early as 1897, "To win over the Dutch . . . you have only to sacrifice 'the nigger' absolutely and the game is easy. . . . (S)elf government . . . and colonial loyalty . . . (required) the abandonment of the black races."[48] Encouraging white unity and peace took precedence over English liberalism, for the Afrikaners had proved themselves capable of protracted violent disruption, while blacks remained divided. The British concluded that Union was achievable only on the "Boers' terms," contrary to expectations among the colored and African populations that a British victory would consolidate reforms.[49]

The historical record preserves a symbolic moment revealing the implications of the whites' nascent coalition. The first draft of the 1902 peace treaty between Afrikaner and British forces promised the subsequent extension of the franchise "to natives." This clause was crossed out by Boer Generals Smuts and Hertzog and replaced by a vague commitment to later discussions of the issue.[50] This amendment was accepted by the British, apparently without discussion. Having grabbed South Africa, the imperial hands of liberal uplift were withdrawn to a regal posture, clasped in back.

Exclusion of the "natives" and later of the "coloreds" would be reinforced during subsequent decades of continued political competition

[46] See, for example, J. A. Hobson, *The War in South Africa* (London: George Allen, 1900).

[47] See, for example, Basil Williams, ed., *The Shelborne Memorandum* (London: Oxford University Press, 1925); Thomas Pakenham, *The Boer War* (New York: Avon, 1979); Monica Wilson and Leonard Thompson, eds., *The Oxford History of South Africa*, vol. 2 (New York: Oxford University Press, 1969).

[48] G. H. L. LeMay, *British Supremacy in South Africa, 1899–1907* (Oxford: Clarendon Press, 1965), 11–12.

[49] Peter Walshe, *The Rise of African Nationalism in South Africa* (Berkeley: University of California Press, 1971), 16. See also Ian Goldin, *Making Race: The Politics and Economics of Coloured Identity in South Africa* (Cape Town: Longman, 1987), 32; Gavin Lewis, *Between the Wire and the Wall* (Cape Town: David Philip, 1987), 15; Donald Denoon, *A Grand Illusion* (London: Longman, 1973), 4, 111.

[50] J. D. Kestell and D. E. van Velden, *The Peace Negotiations* (London: Clay, 1912), 112.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

between English and Afrikaners. Nevertheless, the "game" was not as "easy" as Milner had expected. Policies varied, as different "solutions" were tried and divergent interests acceded to, depending on who was in power. Some "natives" would still be advanced, and "coloreds" enjoyed some preferential treatment, both as instruments of a policy of divide and rule. But these exceptions were subject to overarching discrimination. Still many Afrikaners were not appeased, as indicated by continued Afrikaner nationalism, suspicion of English liberalism, and efforts to further racial domination. By 1936 Afrikaners forced the removal of African voters from the common rolls in the English-dominated Cape. After 1948 the Afrikaners imposed apartheid and then sought to further unify whites against communism and "the black threat." For all this variation, the original "deal" was elaborated, establishing the pattern that "the process of pact-making between the whites [was] at the expense of the blacks and browns."[51] English-Afrikaner competition continued but was contained in a single polity of racial domination.

Much as South African state consolidation faced the impediment of ethnic conflict, state consolidation in the United States faced a corresponding impediment of regional conflict between North and South. The indigenous population of Native Americans would be largely wiped out, but slaves remained numerous and their fate a bone of regional contention. This conflict was initially finessed in the Constitution. The future of Southern slavery was deliberately left unresolved, with the South able to insist on a compromise.[52] Slaves were not freed or given the vote. The South's representation was bolstered by including each adult slave as three-fifths of a person—a political incentive as well to maintain profitable slave labor.[53] Sectional tension over the future and extension of slavery remained but was contained by a further series of compromises and concessions to Southern interests. The Dred Scott decision of 1857, for example, deemed formal guarantees of equality and citizenship rights inapplicable to blacks.[54]

Regional conflict over the future of slavery came to a head in the mid-nineteenth century. The North sought to strengthen and use the federal government to support its early industrialization, to extend the railroads, and most significantly to limit the expansion of slavery.[55]

[51] Pakenham (fn. 47), 612.
[52] Jordan (fn. 10), 332; Richard Kluger, *Simple Justice* (New York: Knopf, 1980), 33.
[53] Dwight Lowell Dumond, *Anti-Slavery* (Ann Arbor: University of Michigan Press, 1961),45.
[54] Eric Foner, *Free Soil, Free Labor, Free Men* (London: Oxford University Press, 1970), 292–93.
[55] Barrington Moore, Jr., *Social Origins of Dictatorship and Democracy* (Boston: Beacon, 1966), 125, 136; Paul Lewinson, *Race, Class and Party* (New York: Grosset and Dunlap, 1932), 26.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Abolitionists joined in pressing for greater political centralization as a means of forcing the end of slavery. The South defended the federalist division of power, which had preserved states' rights, including those regarding slavery and its extension to ensure agricultural profits.[56] As John Quincy Adams had predicted, this conflict could be "settled only at the cannon's mouth,"[57] after institutional accommodations had failed. America's "genius for compromise and conciliation" was cut by the "bloody gash" of the ensuing Civil War, the most violent domestic conflict in American history.[58] The North's victory opened the way for a shift toward more centralized federal power. Indeed, mobilization in the Civil War was a turning point in the state's consolidation, control, and exercise of resources as an emerging global power.[59] In the process, both the North and the South had become increasingly united internally, and that exacerbated the interregional conflict.[60]

The North's victory ensured the legal preservation of the Union sought by Lincoln, but "binding up the nation's wounds" required resolution of the regional conflict and of the status of freed slaves. An effort to deport blacks was attempted but abandoned as impractical. Black enfranchisement under Reconstruction exacerbated regional conflict, raising fears of a renewed Southern rebellion and encouraging another shift of federal policy in search of a "solution." By 1877 compromise had reemerged. The imposition of blacks' rights was abandoned and federal troops were withdrawn from the South, which reduced resistance to national unity.[61]

After Reconstruction a coalition of North and South was fostered by reinforced racial domination, as Fourteenth Amendment guarantees were effectively ignored. Further appeasing the South, the Plessy decision of 1896 reaffirmed states' rights to enact their own rules of racial exclusion applicable also to mulattoes. Jim Crow segregation was enforced throughout the South by the 1890s, in particular after the defeat of the Populist movement. Later, Southern Democrats used their electoral power and vetoes to continually reinforce states' rights in issues of

[56] Kenneth M. Stampp, ed., *The Causes of the Civil War* (New York: Simon and Schuster, 1959), 63.
[57] Ibid., 59.
[58] Moore (fn. 55), 113.
[59] Stephen Skowronek, *Building a New American State* (Cambridge: Cambridge University Press, 1982), 30; Richard F. Bensel, *Yankee Leviathan* (Cambridge: Cambridge University Press, 1990), ix; Ira Katznelson and Aristide Zolberg, eds., *Working-Class Formation* (Princeton: Princeton University Press, 1986), 212; Eric Foner, *Reconstruction* (New York: Harper and Row, 1988), 23.
[60] See, for instance, V. O. Key, Jr., *Southern Politics in State and Nation* (New York: Knopf, 1949).
[61] C. Vann Woodward, *Reunion and Reaction* (Boston: Little Brown, 1951); Barbara J. Fields, "Ideology and Race in American History," in J. Morgan Kousser and James M. McPherson, eds., *Region, Race and Reconstruction* (New York: Oxford University Press, 1982).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

race. The North also practiced de facto segregation. As in South Africa, "the Negro paid a heavy price so that whites could be reunited in a common nationality."[62] More than four thousand blacks (and some whites) who were seen to violate Jim Crow were lynched, while the federal government stood idly by.[63] As described by W. E. B. Du Bois, "All hatred that the whites after the Civil War had for each other gradually concentrated itself on [blacks]."[64]

Comparison of South Africa and the United States suggests important dissimilarities. South Africa's newly forged state authority, bolstered by the strength of the British Empire, enforced segregation from the center in varying and increasingly harsh forms. The potential threat from the African majority impelled such strong intervention. Neither Afrikaner nor English disputed racial domination or centralized power—rather, they competed for control over such power. In the United States the division of power continued to be contested and entangled with disputes over racial domination. After the Civil War the North confidently foisted reforms on the South, but by the end of Reconstruction the North conceded that the Union was still too weak to impose its will and it was unwilling to provoke further conflict by interfering in locally enforced segregation. With "no real fear of a military threat from the black (minority) population,"[65] appeasing the South by tolerating Jim Crow was preferable to the prospect of continued Southern resistance. The federal balance of power was shifted back toward the states, which were left to impose their own racial order. Mobs in turn reinforced that racial order when states did not or could not. Constitutional guarantees of equality were unenforced, whereas in South Africa no such guarantees existed and the state acted with force and impunity.

The reinforcement of racial domination in South Africa and the U.S. followed different paths, but the result was remarkably similar. Major conflict had reinforced distinct solidarity among Afrikaners and English, South and North. The conflict between these ethnic fragments or regions was gradually contained at the expense of blacks, in

[62] Fredrickson (fn. 3), 191. See also C. Vann Woodward, *The Strange Career of Jim Crow* (New York: Oxford University Press, 1955), 65; Moore (fn. 55), 132, 146.

[63] Williamson (fn. 36), 85.

[64] W. E. B. Du Bois, *Black Reconstruction in America, 1860–1880* (New York: Athenaeum, 1992), 125.

[65] George Reid Andrews, "Review Essay: Comparing the Comparers: White Supremacy in the United States and South Africa," *Journal of Social History* 20 (1987), 589; Richard M. Valelly, "Party, Coercion, and Inclusion: The Two Reconstructions of the South's Electoral Politics," *Politics and Society* 21 (March 1993).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

accordance with Denoon's "golden law . . . that every white bargain must be sealed by an African sacrifice."[66] In the "moments of madness"[67] capping cataclysmic and violent change, racial segregation was enforced or allowed. Racial distinctions imbedded in the past were prominently "available" to diminish the regional or ethnic conflict that impeded consolidation of the nation-state. Reinforcing legal discrimination encouraged the unity of whites as dominant over blacks. Continued intrawhite tension reinforced this "solution." The potential for a coalition among progressive whites and blacks was ignored or abandoned.

The contrast with Brazil is here particularly useful. Portuguese colonialism had imposed on Brazil a more unified central authority than that which developed in South Africa or the United States. The withdrawal of Dutch invaders after 1654 left no competing European fragment akin to the Afrikaners in South Africa. Emerging nationalism and tensions within Brazil were muted by the arrival in 1808 of the Portuguese court, forced to flee from Napoleon. Popular descendants of the Portuguese crown continued to rule over Brazil for eighty years, overseeing a peaceful transition from colony to independent empire and appeasing British interests enough to avoid direct conquest. Economic development remained slow, elites retained their centralized focus, and nationwide slavery was gradually and peacefully abolished. As a result, there was relatively little impetus for conflicts that might otherwise have undermined state consolidation and capacity. The occasional small provincial revolt was contained by compromise. "Clientalist" and "patrimonial" rule was never seriously challenged.[68]

In Brazil a prefabricated central state was in place when the winds of modernity hit. As a result, "Brazil is famous for its 'white,' or peaceful revolutions," having managed smooth transitions from empire to republic, and from slavery to abolition, in 1888–89.[69] Race did not become a political football in regional or ethnic conflict. There was no cataclysmic internal war comparable to that of the United States or later South Africa. Indeed, Brazilians were eager to avoid the sort of conflict over slavery and race that they had seen nearly tear apart the United States. And having avoided such a conflict, there was no need for the sort of reconciliation elsewhere encouraged through a white coalition and an explicit ideology of racial discrimination.[70]

[66] Denoon (fn. 49), 158.
[67] Aristide Zolberg, "Moments of Madness," *Politics and Society* 2 (1978).
[68] See Riordan Roett, *Brazil: Politics in a Patrimonial Society* (New York: Praeger, 1984).
[69] Gilberto Freyre, *Brazil: An Interpretation* (New York: Knopf, 1945), 120.
[70] See Donald Pierson, *Negroes in Brazil* (Chicago: University of Chicago Press, 1942), 335.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

The postabolition Brazilian state eschewed legal discrimination and encouraged unity among Brazilians of any color (ostensibly including native "Indians"). Having experienced larger slave revolts, the Brazilian elite was more fearful of blacks than their U.S. or South African counterparts. They were eager to submerge potential racial conflict under the myth of "racial democracy" and images of an inclusive nation and corporatist state.[71] This process was debated and blacks were excluded from immigration.[72] But within the country, no rules of racial exclusion were imposed. Rather than reinforce past images of racial inferiority and domination, this legacy was reinterpreted as a benign Luso-tropical tolerance. Inherited and continued racial inequality was denied or camouflaged as reflecting unavoidable but fluid class distinctions.

In the absence of formal segregation, accommodation was encouraged. A few Afro-Brazilians were able to advance themselves. Further miscegenation was encouraged to "whiten" and unite the population. Mulattoes were not forced into black unity by official segregation. Racial categories were removed from the census and studies of discrimination were outlawed, so as to obviate any challenges to the myth of racial democracy. Many blacks were deprived of the franchise, but on the basis of illiteracy, not race per se. Eventually this voting qualification was abandoned, after literacy rates had risen. Racial discrimination was later outlawed, although no violations were prosecuted. Conflict was avoided and development proceeded.

It is worth noting that the Brazilian idea of "racial democracy" was advocated for adoption in the United States during the early twentieth century, but found inapplicable. No less a figure than Teddy Roosevelt traveled to Brazil, noted that the U.S. and Brazil both had "mixed" populations, and commented on "the tendency of Brazil to absorb the Negro. . . . [T]hese white men draw no line against the Negro." Roosevelt approvingly cited the remarks of a Brazilian: "You of the United States are keeping the blacks as an entirely separate element. . . . They will remain a menacing element in your civilization. . . . [The alternative] we Brazilians have chosen will in the long run, from the national standpoint, prove less disadvantageous."[73] But the United States was not then free to choose this alternative, for the die had already been cast in a bloody mold. Abandoning the ideology of racial domination might very well have reopened the wounds that had already once torn apart

[71] See Thomas E. Skidmore, *Black into White: Race and Nationality in Brazilian Thought* (New York: Oxford University Press, 1974).

[72] Celia Marinho de Azevedo, *Onda Negra, Medo Branco* (Rio de Janeiro: Paz e Terra, 1987).

[73] Theodore Roosevelt, "Brazil and the Negro," *Outlook* 106 (February 21, 1914), 409–11.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

the republic and then threatened to do so again during Reconstruction. Poor whites insisted on asserting their racial superiority, and elites in the North and South were eager to avoid class conflict by projecting white racial unity. Acceptance of the "disadvantages" of explicit racial domination had been established by the trajectory of American history, as it also had been in South Africa.

## Mobilization Responses to Race-Making

The primary focus of this paper is to demonstrate that official postabolition racial domination or the absence of it was prominently connected to the impetus for building the nation-state. But if such an analysis is to prove robust, it should also help explain variations in resulting mobilization and conflict; that is, social construction of explicit racial domination and social movements by the victims of such domination should logically be connected. I will now consider whether that indeed is the case—whether mobilization and conflict "from below" can be explained according to policies of domination imposed "from above."

Institutionalized domination setting legal boundaries of race also consolidates subordinated racial identity as a potential basis for resistance. Imposed discrimination encourages group solidarity among blacks whose fate is so linked.[74] This process of identity formation logically precedes and then shapes the logic by which resources and political opportunities are acted upon.[75] In Karl Marx's terms, a group must self-consciously exist "in itself" before it can act "for itself."[76] State policy helped forge such group self-consciousness among blacks, establishing the "who" that then interpreted and responded to structural conditions accordingly. But even when race becomes a salient identity, it does not necessarily lead to mobilization. And its form varies wherever or whenever such mobilization emerges. Such uncertain and fluid responses are connected to variations in racial domination.

Racial exclusion beneficial to whites in the short run may provoke countermobilization in the long run, whereas lack of such formal exclusion curtails mobilization and leaves inequality unchallenged. For instance, apartheid in South Africa and Jim Crow in the United States encouraged black solidarity, with forms of protest varying according to

[74] See Michael Dawson, *Behind the Mule* (Princeton: Princeton University Press, 1994).
[75] See Sidney Tarrow, *Power in Movement* (Cambridge: Cambridge University Press, 1994).
[76] Karl Marx, "The Poverty of Philosophy," in David McLellan, ed., *Karl Marx: Selected Writings* (Oxford: Oxford University Press, 1977), 214.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

shifts in state policy. Reforms invited more moderate mobilization, often aimed at integration. The reversal or absence of reforms provoked more militant protest and often separatism. "Racial democracy" in Brazil elicited more muted racial identity and mobilization, even during periods of reform and despite evident inequality, resources, and opportunities for protest. Yet even in Brazil limited forms of protest reflected changes in state rule. The previous dependent variable of official racial domination can be reconfigured into an independent variable to explain such emergence and various forms of mobilization.

In South Africa early and less rigid forms of state discrimination produced limited and moderate mobilization, with more militant popular opposition emerging only with the increasing reinforcement of segregation. Before Union, indigenous resistance remained divided. The African National Congress (ANC) was founded to unify Africans shortly after the newly created Union began to refine discrimination. But the ANC remained small, elitist, and polite in its petitioning. Continued conflict between English speakers and Afrikaners ushered in a more strictly segregationist government in 1924 under Hertzog, who later deprived coloreds of much of their relative privilege. Like later Afrikaner nationalists, Hertzog sought to trump the racial segregation of the English and their allies in order to further consolidate Afrikanerdom. Tightening segregation unified Africans and coloreds across class and region as common victims of racial domination, provoking greater resistance.

After 1948 the Nationalist government formalized Afrikaner rule and even stricter segregation under apartheid, further solidifying subordinate racial identity. The ANC and its more radical offshoot, Pan Africanist Congress, gained massive support for more militant protests aimed at defeating, not just reforming, the state.[77] In the 1970s the Black Consciousness movement responded to a tightening of apartheid with calls for black separatism that would unite "Africans, coloreds, and Asians." In the 1980s the United Democratic Front responded to halting reforms with more integrated mass mobilization. With no constitutional guarantees to appeal to, opponents of the state demanded more radical change. In 1990, under pressure from continued mass mobilization, internal splits, economic dislocation, sanctions, and the end of the cold war, the state announced its intention to abandon apartheid. The

[77] See Saul DuBow, *Racial Segregation and the Origins of Apartheid in South Africa, 1919–36* (Hampshire, England: Macmillan, 1989); Tom Lodge, *Black Politics in South Africa since 1945* (Johannesburg: Ravan, 1983).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

majority of the opposition took up the invitation to engage in negotiations.[78]

Racial mobilization in the United States followed a similar overall pattern, though with complex differences. Early post-Reconstruction discrimination provoked limited mobilization. Regional differences remained, unaltered by relatively constant federal policies of neglect. Repression in the South encouraged Booker T. Washington's accommodationism, while deprivation in urban areas of the more liberal North evoked the militant views of W. E. B. Du Bois. Disappointment over the lack of reforms after the First World War provoked the mass movement of Marcus Garvey in the North but nothing comparable in the South.[79] With the New Deal and the Second World War, the central United States authority expanded its social intervention, raising the prospects of reform. The cold war also raised concerns about the international reputation of the U.S.

U.S. federal reform at midcentury encouraged black solidarity across class and region. Having developed the capacity to impose its will, federal authorities hesitantly began to revisit the contentious issues of reforming Jim Crow. The most notable signal of this shift was the 1954 Supreme Court decision, *Brown* v. *Board of Education*. Such state action provided an opening for the civil rights movement, which gained its initial mass following in the legally segregated South. Calling on the nation to live up to the ideals of the Constitution, relatively moderate forms of mobilization pushed for further federal intervention against Jim Crow. Southern activism then inspired blacks in the North. Their anger at continued deprivation, less easily alleviated by federal intervention, led to riots and more militant forms of black nationalism.[80]

The Brazilian case is striking for its lack of significant race-specific mobilization. Socioeconomic inequality and informal discrimination according to physical differences continued after slavery but were not sufficient to engender strong subordinate racial identity or massive protest. The lack of an official ideology and policy of racism was crucial. However, within that constraint, even the limited forms of Afro-

[78] See Anthony W. Marx, *Lessons of Struggle* (New York: Oxford University Press, 1992); Heribert Adam and Kogila Moodley, *The Opening of the Apartheid Mind* (Berkeley: University of California Press, 1993).

[79] See August Meier et al., eds., *Black Protest Thought in the Twentieth Century* (New York: Macmillan, 1971).

[80] The literature here is vast. See Doug McAdam, *Political Process and the Development of Black Insurgency, 1930–1970* (Chicago: University of Chicago Press, 1982); Aldon D. Morris, *The Origins of the Civil Rights Movements* (New York: Free Press, 1984); John T. McCartney, *Black Power Ideologies* (Philadelphia: Temple University Press, 1992).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Brazilian mobilization responded to shifting state policy. In the 1930s the Vargas regime reconsolidated central state authority, which had diminished during the Federal Republic after 1889. Vargas affirmed his commitment to racial democracy. The relatively moderate Frente Negra largely supported the regime. In the 1970s, when continued socioeconomic deprivation among blacks flew in the face of the official doctrine of "tolerance," images of the U.S. civil rights and black power movements spread to Brazil. The more militant Movimento Negro Unificado emerged, though it still had only limited popular support.[81]

## "Unmaking" Racial Domination

The recent demolition of the legal edifice of racial discrimination in South Africa and the United States also can be explained, albeit briefly, by reference to the dynamics of race-making. Economic costs of discrimination, changing international pressures, and most prominently popular protest all contributed to forcing the end of legal segregation. However, in both cases reform would have been stymied had militarily strong, central state authority retained an ideological and strategic commitment to enforcing or allowing racial domination. With the greater resolution of prior regional and ethnic conflict, the impetus to encourage white unity via racial domination had become less pressing. Defusing the resulting "black-white" conflict became more pressing. The end of legal subordination thus came despite continued white resistance, but only after the logic of race-making was reversed by further developments.

In the United States the South had been appeased by allowing formal racial discrimination on the local level. By midcentury industrialization and prosperity had begun to spread to the South,[82] which had earlier regained its political foothold in Washington and abandoned all thought of secession. The South had been "Americanized."[83] This process had allowed for greater central state consolidation and white national unity to be largely achieved. The federal balance of power was gradually reconfigured toward the center. Meanwhile, despite Southern resistance, increased black protest encouraged by and pushing for fur-

[81] See Lélia Gonzalez and Carlos Hasenbalg, *Lugar de Negro* (Rio de Janeiro: Marco Zero, 1982); Michael Hanchard, *Orpheus and Power* (Princeton: Princeton University Press, 1994).

[82] U.S. Department of the Census, *Historical Statistics of the United States* (Washington, D.C.: U.S. Government Printing Office, 1975), series F-297–348, pp. 243–45, 295; Gavin Wright, *Old South, New South* (New York: Basic Books, 1986).

[83] Myrdal (fn. 35), 1011.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ther reforms, pressed for the application of central power against localized racial policies.

By midcentury the centralized American polity had become strong enough to intervene in the historically most contentious and last bastion of states' rights. The Union victory in the Civil War was finally consolidated a century later with a "second Reconstruction," in which the die of racial order was remolded. Black Southerners recognized this shift toward renewed federal action, welcoming representatives of the U.S. Commission on Civil Rights in 1958 with the remark that at last "the Big Government has come."[84] Regional tensions that had encouraged a white supremacist coalition remained. But this conflict among whites was gradually diminished by racial domination and replaced as the most pressing threat to national unity by the "black-white" conflict it had engendered. To curtail the rising political and economic disruption of black protest, official racial domination was ended by strong action from the center; social discrimination persisted, however.

Conflict among whites also diminished in South Africa, albeit later than in the U.S. Post-1948 Afrikaner control of an increasingly strong South African state had reinforced Afrikaner culture and language. State intervention and employment (to administer apartheid) brought greater economic parity with the English. For example, the proportion of Afrikaners working in white-collar jobs rose from 29 percent in 1946 to 65.2 percent in 1977.[85] As a result, "the Afrikaner had acquired more self-confidence; English and Afrikaner have grown together," thereby diminishing Afrikaner "fear of the English using non-white votes to strengthen their position."[86] Conflict between Afrikaners and English thus lessened as a central political concern, which had previously encouraged the use of segregation as a means of unifying whites.

As the costs of legal segregation rose, white South Africans eventually agreed to end apartheid, requiring a more fundamental political transition than in the U.S. Major black protest, elite division, sanctions, and lost opportunities for market growth had all taken their toll. With whites increasingly dependent on blacks, these costs became unbearable. By 1992 F. W. de Klerk was able to win an astonishing 68.7 percent of the combined Afrikaner and English vote for a referendum supporting negotiations aimed at ending minority rule. Whites em-

[84] Harris Wofford, *Of Kennedys and Kings* (New York: Farrar, Strauss and Giroux, 1980), 467.

[85] Heribert Adam and Hermann Giliomee, *Ethnic Power Mobilized* (New Haven: Yale University Press, 1979), 169–75. See also Donald L. Horowitz, *A Democratic South Africa?* (Berkeley: University of California Press, 1991), 79–81.

[86] Author interview with Gerrit Viljoen, Pretoria, April 28, 1994.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

braced the reassuring prospect of a de Klerk-Mandela "partnership," with English voters increasingly supporting a reformist National Party.[87] The white coalition had taken hold, and white privilege was further consolidated. Black protest had by then replaced the English-Afrikaner conflict as the dominant threat to peace. Official racial domination had worked and then backfired, and was finally abandoned, despite white right-wing resistance. Furthermore, because the South African state had been more explicitly designed on the basis of racial domination, this transition required a new constitution. By contrast, United States central authority had imposed reform according to constitutional interpretation and edict.

The same process of ending racial domination was not applicable to Brazil, because no comparable racial order had been constructed. Subordinate racial identity had no unifying target of official policy against which to mobilize, and no formal racial domination had to be reformed. This does not mean that social discrimination or economic inequality was less evident in Brazil. To the contrary—the lack of an official racial order that might have provoked stronger mobilization has left such discrimination largely unchanged.

## Implications

Race-making had no single determinant, but its origins and consequences can be specified. In the three cases compared here, pervasive inequality and images of primordial inferiority were the heritage of slavery but were encoded in varying forms after abolition. Miscegenation influenced racial distinctions and the potential for conflict, but a continuum of skin colors was subject to shifting official categories. Competing class interests were appeased by various forms of discrimination. Race then appears less fixed than if it were preordained by culture, slavery, ancestry, or specific economic interests. Interpretations of historical legacies and interests have varied according to evolving racial orders reinforcing nation-state consolidation, stability, and development. Racial domination, categories, and conflict appear to be as fluid as those emerging dynamics of coalition building that shaped them.

The power of this explanation of race-making lies in its ability to help account for extensive variations in social constructions of race. In Brazil the lack of regional or ethnic conflict is consistent with the rela-

[87] Adam and Moodley (fn. 78), 2; Timothy D. Sisk, *Democratization in South Africa* (Princeton: Princeton University Press, 1995), 137.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tive absence of racial ideology, official categorization, or conflict. For South Africa and the United States, the state's elaboration of racial domination was shaped by conflict among whites, who gradually sought to reconcile their conflict by unifying as whites and reinforcing exclusion of blacks. "War (was) continued by other means." To instill "peace in civil society, . . . political powers . . . re-inscribe . . . inequalities," in these instances along lines of race.[88] Continued iterations of "intrawhite" political or economic competition repeatedly reinforced racial domination. These processes played themselves out during the century-long era of nation-state building, amid variations of policy.

These dynamics follow more general patterns. For instance, Rogers Brubaker has argued that historical German disunity was resolved through the construction of an exclusive ethnic citizenship. Earlier French state consolidation allowed for a more inclusive civic form of nationalism, evident in state policy if not current social practice.[89] In South Africa, the United States, and Brazil, colonialism, slavery, and geography had left a substantial and historically differentiated black population. Race then figured prominently in the definition and consolidation of the nation-state. Disunity in South Africa and the U.S. was resolved through exclusive race-specific nationalism and citizenship, which did not develop in relatively unified Brazil. War played a central role in these processes. In Europe, foreign wars requiring conscription produced demands for the expansion of citizenship.[90] Resolution of internal wars in the U.S. and South Africa similarly extended citizenship rights for whites in a unified polity, but it also reinforced black exclusion.

The state emerges as a central actor in race-making, as it is the subject of contestation and responds to various challenges from the society in which it is embedded. To dilute internal conflict and encourage national unity, racial domination was officially reinforced in South Africa and the U.S., and racial antagonism was consistently avoided in Brazil. Apartheid or Jim Crow then provoked the antithesis of black protest. Conflict among whites had gradually diminished at the cost of rising black-white conflict. To contain this new conflict, the state then moved to synthesize a more inclusive racial order, abandoning official racial domination. Throughout, these states acted with relative autonomy, responding to assertions of interest with appeasement, compromise, or

[88] Michel Foucault, *Power/Knowledge* (New York: Pantheon, 1972), 90.

[89] Brubaker, *Citizenship and Nationhood in France and Germany* (Cambridge: Harvard University Press, 1992).

[90] Charles Tilly, *Coercion, Capital and European States* (Cambridge: Blackwell, 1990).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

co-optation. The state-led process of nation-building (and the defining of citizenship) shaped and reshaped the racial order. Amid missteps, local and national division, and unintended consequences, state actions reflected intentional responses to pressing concerns.

I hope not to be misunderstood about the implications of this analysis. That intrawhite conflicts encouraged an explicit ideology and rule of discrimination against blacks does not mean that with the greater resolution of such conflict racism has disappeared or will do so. Whites in South Africa and the United States benefited from defining themselves as such, with the state reinforcing racism in varying forms of postabolition segregation. But once race has been so constructed, the state cannot easily dismantle its awful creation. "Social structures, types and attitudes are coins that do not readily melt. Once they are formed they persist."[91]

Racial identities, ingrained through painful experience and imbedded in everyday life, do not quickly fade even if the conditions that reinforced them change. In the United States legal discrimination has ended, but discrimination remains and race reforms have recently come under threat as a concomitant of resurgent states' rights. Racial identities have remained salient, not least because the African American minority views its solidarity as a vital resource. The same may now come to be true in postapartheid South Africa. The previous ideological project of interpreting culture, ancestry, and economic interests according to race has left deep scars. Even in Brazil nascent racial identity and conflict encouraged by information about the former two cases remains evident. That whites constructed race as a means of domination does not mean that racial identity cannot then be embraced by subordinates for their own advantage. Indeed, that has been the case.

What emerges is a consistent pattern of efforts at conflict resolution and coalition building as a central component of racial dynamics. Nation-state builders in the United States and South Africa sought to resolve conflict among whites by building a coalition of domination over blacks, thereby diminishing the most viable threat to the state and economy. Boundaries of racial category and enforced discrimination were constructed and historical legacies interpreted accordingly. The nation emerged as an "imagined community."[92] Who was included or excluded did not emerge spontaneously, however, but rather was reinforced by official policy. The unintended result was heightened mobi-

[91] Joseph Schumpeter, *Capitalism, Socialism and Democracy* (New York: Harper, 1947), 12–13.
[92] Benedict Anderson, *Imagined Communities* (London: Verso, 1983).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

lization by blacks unified by their exclusion, with black protest eventually forcing a reconfiguration of the nation-state as inclusive, albeit still torn by the legacy of racial antagonism. Institutions of domination reinforced assertions of racial identity, which then forced a reconfiguration of institutions. But resulting identity remains. Brazil confirms this pattern by its relative lack of "intrawhite" conflict, its avoidance of racial domination or conflict, and the lower salience of racial identity. Strategic calculations differed, either encouraging racial domination and conflict or not, but the imperative of nation-state consolidation was evident in each situation. The evolution of Du Bois's "problem of the color line" during this century was inextricably connected to the political dynamics of conflict resolution or avoidance framed by the ideal of the nation-state.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# THE BREAKDOWN OF HIERARCHIES IN THE SOVIET UNION AND CHINA

## A Neoinstitutional Perspective

By STEVEN L. SOLNICK*

WHY did modest attempts to decentralize the centrally administered Soviet system lead to its collapse, while in China more far-reaching decentralization left central political and administrative hierarchies relatively intact?

A growing number of authors have scoured the Soviet/Russian and Chinese reform experiences in search of lessons about the relative merits of rapid versus evolutionary reform.[1] Though these authors often arrive at radically different conclusions, most agree that "a gradual strategy requires effective state management of the economy" and that the relative effectiveness of the Chinese state in managing reforms in that country can be attributed to its postponement of political reforms.[2] This article rejects the assumption that organizational integrity and effectiveness is exogenous to the process of reform, and it examines the specific processes that undermined or preserved institutional stability in these two reform environments. The analysis suggests that organiza-

* Portions of this research were supported by IREX and the Harvard Academy for International and Area Studies. The author is grateful to Tom Bernstein, Scott Bruckner, Andrew Cortell, Mark Groombridge, Joel Hellman, Bob Jervis, Ira Katznelson, Bob Keohane, Ron Rogowski, Ken Shepsle, Dorothy Solinger, Debora Spar, and Jack Snyder for thoughtful and constructive comments on previous drafts.

[1] See, for example, Alan Gelb, Gary Jefferson, and Inderjit Singh, "Can Communist Economies Transform Gradually: The Experience of China," in Olivier Blanchard and Stanley Fischer, eds., *NBER Macroeconomics Annual 1993* (Cambridge: MIT Press, 1993); John McMillan and Barry Naughton, "How to Reform a Planned Economy: Lessons from China," *Oxford Review of Economic Policy* 8 (Spring 1992); Ronald I. McKinnon, "Gradual versus Rapid Liberalization in Socialist Economies: The Problem of Macroeconomic Control," including comments by Anders Åslund and Jacek Rostowski, *Proceedings of the World Bank Annual Conference on Development Economics* (1993); Jeffrey Sachs and W. T. Woo, "Structural Factors in the Economic Reforms of China, Eastern Europe and the Former Soviet Union," *Economic Policy* 18 (April 1994); Wing Thye Woo, "The Art of Reforming Centrally Planned Economies: Comparing China, Poland, and Russia," *Journal of Comparative Economics* 18 (June 1994).

[2] Gelb, Jefferson, and Singh (fn. 1), 128. They refer to this rather imprecisely as "perestroika" before "glasnost'." Such a formulation implies that this separation and sequencing of political and economic reform is the result of explicit choices by central authorities.

*World Politics* 48 (January 1996), 209–38

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tional reforms in the Soviet Union radically weakened authority links within Soviet hierarchies and accelerated the process of organizational disintegration—thus making a gradualist approach impossible—whereas superficially similar reforms in China left fundamental authority linkages intact.[3]

Previous organizational analyses of centrally planned systems treated internal structure as a causal variable, responsible for inefficiencies like resource hoarding and for poor institutional performance.[4] These analyses did not suggest how poor performance could under certain circumstances affect or even undermine structure. In this article, I draw on the literature on the economics of institutions to discuss how reforms emphasizing decentralization of decision making upset the offsetting asymmetries of information and authority within the bureaucracies of centrally planed systems. I also consider how bureaucratic supervisors might forestall this authority imbalance by investing in their long-term reputation as disciplinarians.

By extending neoinstitutional analysis to environments characterized by uncertain property rights and ambiguous performance measures, I suggest how theories initially developed to explain the emergence of institutional structures can help account for their breakdown. The ultimate fragility of Soviet institutions, in comparison with the resilience of Chinese institutions, may also offer important insights into the behavior of actors in the post-Soviet environment or in other postcommunist societies.

I begin by introducing a simple model of a Soviet-type bureaucratic hierarchy utilizing some key concepts from principal-agent theory. I then introduce the metaphor of a bank run to discuss how changes to

[3] Another analysis suggesting that the nature of political and economic reforms could directly undermine state capacities is Victor Nee and Peng Lian, "Sleeping with the Enemy: A Dynamic Model of Declining Political Commitment in State Socialism," *Theory and Society* 23 (April 1994). Nee and Lian argue that political reform in the Soviet Union proceeded "too quickly, so that monitoring capacity weakened greatly," an assessment that is wholly consistent with the model presented here.

[4] Bureaucratic models were particularly prevalent in studies of Soviet industrial planning and management. These works tended to emphasize the coordination problems inherent in any system of central planning and the consequent perverse incentives faced by industrial managers. See, for instance, Joseph S. Berliner, *Factory and Manager in the USSR* (Cambridge: Harvard University Press, 1957); Edward A. Hewett, *Reforming the Soviet Economy: Equality versus Efficiency* (Washington, D.C.: Brookings Institution, 1988); Alec Nove, *The Soviet Economic System* (Boston: Allen and Unwin, 1980); János Kornai, *The Socialist System: The Political Economy of Communism* (Princeton: Princeton University Press, 1992); and Thane Gustafson, *Crisis amid Plenty: The Politics of Soviet Energy under Brezhnev and Gorbachev* (Princeton: Princeton University Press, 1989). Political scientists extended organizational analyses into more general models of the Soviet system, with an analogous emphasis on the nature of "informal adjustive mechanisms" employed by actors to compensate for the fundamental weaknesses of overbureaucratization. For a synoptic review of this literature, see Jerry F. Hough, "The Bureaucratic Model and the Nature of the Soviet System," in Hough, ed., *The Soviet Union and Social Science Theory* (Cambridge: Harvard University Press, 1977).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

the institutional environment that offered local actors greater autonomy could produce widespread defections by agents. I also use simple insights from game theory to consider how strategic choices by principals might have led to alternative outcomes.

Finally, I apply this model to attempts to devolve authority to lower levels of political, economic, and state structures in the Soviet Union and China. I consider why superficially similar reforms caused the central organizations in the former to fragment and disintegrate, but allowed those in the latter to survive and exert continuing control over the course of economic reforms. In the Soviet case bureaucratic supervisors found their authority undermined, as subordinates utilized their control over information to mask the expropriation of organizational assets. In China, I argue, hierarchical authority has been preserved (thus far) because political leaders guarded their mechanisms and reputations for rule enforcement and because the nature of post-Mao property rights created disincentives to outright defection from state hierarchies.

## I. A Neoinstitutional Model of a Soviet-type Bureaucracy

Issues of authority and obedience are most directly addressed in the economic literature on principals and agents. In this section I offer a basic application of principal-agent theory to a Soviet-type bureaucracy and then consider how the resulting model differs from more traditional models of complex hierarchies.

### The Basic Model

Any complex hierarchy can be thought of as a chain of linked principal-agent relationships in which "each individual in a hierarchical structure, except at the ultimate levels, is simultaneously a principal and an agent when rights are transferred down the organizational ladder."[5] In all but the most trivial agency relationships, agents know more about their own performance than do their principals. Two types of agency problems arise from this information asymmetry: "hidden action" and "hidden information."[6] These categories relate schematically to how hard or

[5] Thráinn Eggertsson, *Economic Behavior and Institutions* (New York: Cambridge University Press, 1990), 41. See also Jean Tirole, "Hierarchies and Bureaucracies: On the Role of Collusion in Organizations," *Journal of Law, Economics and Organization* 2, no. 2 (1986).

[6] Kenneth Arrow, "The Economics of Agency," in John Pratt and Richard Zeckhauser, eds., *Principals and Agents: The Structure of Business* (Boston: Harvard Business School Press, 1985), 38–40. For a review of the basic literature on agency, see Joseph E. Stiglitz, "Principal and Agent," in John Eatwell, Murray Milgate, and Peter Newman, eds., *The New Palgrave: Allocation, Information and Markets* (New

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

honestly the agent is working (hidden action) and to what the maximum output level is, given random factors and the agent's structural constraints (hidden information).

Soviet-type central planning addressed the problem of hidden action by specifying precise output targets judged by planners to correspond to maximum effort and optimal utilization of given inputs. Meeting these plan targets naturally became agents' sole objectives, and nonmonitored activities were subordinated to plan fulfillment. In practice, this meant that Soviet reforms (economic and otherwise) often focused on redefining the set of target indicators both to minimize the losses incurred as a result of such goal displacement and to develop a more easily monitored set of performance measures.[7]

Use of forcing performance targets still presumes reliable estimates of agents' actual performance potential. This potential, however, is hidden information, accurately known only by the agents themselves. In any public bureaucracy—and especially in centrally planned systems—target setting is also complicated by the difficulty of devising accurate measures of organizational outputs.[8]

One alternative to guessing future performance capacities is to utilize information on the past performance of agents to set output targets. This approach, however, leads to the so-called ratchet problem, in which principals continuously adjust targets to reflect the performance of the agent in the most recent period. This creates strong disincentives for agents to demonstrate their true productive potential.[9]

---

York: W. W. Norton, 1989); David E. M. Sappington, "Incentives in Principal-Agent Relationships," *Journal of Economic Perspectives* 5, no. 2 (1991); and Eggertsson (fn. 5), 40–45. Analyses of the principal's problem that stress asymmetric information—and the resultant need to restrain the agent from opportunistically exploiting this information advantage—include Gary Miller, *Managerial Dilemmas: The Political Economy of Hierarchy* (New York: Cambridge University Press, 1992); and Stephen Ross, "The Economic Theory of Agency: The Principal's Problem," *American Economic Review* 63 (May 1973).

[7] Kornai, for instance, describes four typical indicator-adjustment strategies employed by reformers seeking to "perfect" the planning system; see Kornai (fn. 4), 405.

[8] Anthony Downs considered the fact that "the major portion of its output is not directly or indirectly evaluated in any markets external to the organization by means of voluntary quid pro quo transactions" to be a defining feature of any bureau. See Downs, *Inside Bureaucracy* (Boston: Little, Brown, 1967), 26.

[9] John M. Litwack, "Ratcheting and Economic Reform in the USSR," *Journal of Comparative Economics* 14 (June 1990); idem, "Discretionary Behavior and Soviet Economic Reform," *Soviet Studies* 43, no. 2 (1991). Though prominent in discussions of centrally planned economies, Litwack argues that the "ratchet problem" occurs in any principal-agent model featuring asymmetric information, in which principals "cannot or do not commit themselves to long-run incentive schemes or tax schedules." Where present, the ratchet problem invalidates the assumption of Niskanen and others that bureau chiefs can be modeled as budget maximizers. See William A. Niskanen, *Bureaucracy and Representative Government* (Chicago: Aldine, 1971).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

The ratchet effect has often been interpreted as meaning that agents had little incentive (or even had disincentives) to innovate under central planning, but this is not entirely accurate.[10] Since agents had wide latitude over activities not covered by concrete targets, agents often found it in their interest to improvise or innovate to secure a "safety margin," *provided* this innovation did not become known to principals (who would use it to ratchet up performance targets). In fact, the system provided powerful incentives for initiative on the part of enterprise managers or local officials, as long as they maintained control over the rate at which the effects of innovation became known.[11]

This manipulation of field-level performance data was possible because the central planning system was used both to set mandatory performance targets and to verify whether these targets were being met. Reports filed by agents themselves provided the primary means of monitoring target compliance. Any new information about the ability of agents to meet or surpass these targets would force the renegotiation of targets, and this went on continuously in all bureaucratic organizations.

The prevalence of continuous bargaining between principals and agents suggests that contracting between them cannot be modeled as a one-shot operation.[12] If principal-agent relationships are dynamically modeled as a string of short-term agency contracts, subject to ongoing renegotiation, the problem then resembles an iterated game.[13] Within this framework, an effective incentive structure might be based upon agents' average performance over time, and repetition of the game can discourage shirking. There are important conditions, however: principals must be capable of committing to a long-term compensation mechanism; agents for their part must neither discount future payoffs

[10] See, for instance, Joseph Berliner, *The Innovation Decision in Soviet Industry* (Cambridge: MIT Press, 1976), 404, 440; or Peter Rutland, "Economic Management and Reform," in Alex Pravda, Stephen White, and Zvi Gitelman, eds., *Developments in Soviet Politics* (Durham, N.C.: Duke University Press, 1990), 168.

[11] For the demonstration of this assertion for the case of utility-maximizing agents facing the financial and planning environments common to Soviet enterprise managers, see Eirik G. Furubotn and Svetozar Pejovich, "The Soviet Manager and Innovation: A Behavioral Model of the Soviet Firm," in Furubotn and Pejovich, eds., *The Economics of Property Rights* (Cambridge, Mass.: Ballinger, 1974). James Dearden, Barry Ickes, and Larry Samuelson reach related conclusions by distinguishing between incentives for agents to innovate (which can be significant) and the incentives for them to adopt innovations once they become publicly available (which are less powerful). See Dearden, Ickes, and Samuelson, "To Innovate or Not to Innovate: Incentives and Innovation in Hierarchies," *American Economic Review* 80 (December 1990).

[12] Michael C. Jensen and William Meckling, "Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure," *Journal of Financial Economics* 3 (October 1976), 351.

[13] See, for instance, Roy Radner, "Repeated Principal-Agent Games with Discounting," *Econometrica* 53 (September 1985); Jean Tirole, "The Multicontract Organization," *Canadian Journal of Economics* 21 (August 1988); Drew Fudenberg, Bengt Holmstrom, and Paul Milgrom, "Short Term Contracts and Long Term Relationships," *Journal of Economic Theory* 51 (June 1990).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

nor perceive limits to the duration of the agency relationship, and they must not have access to external sources of credit.[14] Violation of the first condition gives rise to the ratchet problem; violation of the second and third conditions becomes more significant at times of reorganization or heightened uncertainty.

## Adjustments to Standard Neoinstitutional Frameworks

Hierarchical relations in Soviet-type bureaucracies demand a reconsideration of certain basic neoinstitutional propositions. In particular, I wish to reexamine some theoretical assumptions in three areas: property rights, authority relations, and risk sharing.

### PROPERTY RIGHTS

An agency relationship is based on the understanding that the principal owns and the agent manages any resources covered by the contract between them. The agent's ability to exercise temporary property rights over these resources (by convention, use rights, income rights, and transfer rights) depends fundamentally on the delegation of those rights from the principal.[15]

Property rights determine more than just the distribution of the assets or resources in question. In a fundamental sense, they frame the issues of power and control central to any hierarchical relationship. As Arrow notes, "An employment contract is precisely a contract on the part of an employee to accept authority."[16] That authority depends on clearly delineated property rights, allowing the principal to transfer actual control over resources without sacrificing ownership.

In practice, all rights delegated through institutional hierarchies in communist systems were based upon the assumption of the Party's unchallenged hegemony. Top Party leaders could delegate authority for setting planning targets or approving personnel appointments to subordinate organizational levels because their ultimate authority—their ultimate "ownership" of all political and economic resources—remained unchallenged. In the absence of clear legal or procedural norms for third-party resolution of property rights conflicts (and the Soviet system clearly lacked these), the principle of ownership could only be

[14] These findings are nicely summarized in Sappington (fn. 6), 59.

[15] The literature on economics of property rights is extensive; see Eggertsson (fn. 5), 33–37, for a review of basic principles. In this discussion, I reject the assertion made by Barzel that a "property rights approach" is somehow distinct and separate from "agency theory." See Yoram Barzel, *Economic Analysis of Property Rights* (Cambridge: Cambridge University Press, 1989), 11.

[16] Kenneth J. Arrow, *The Limits of Organization* (New York: W. W. Norton, 1974), 64. He is paraphrasing Herbert Simon.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

demonstrated by the fact of control.[17] Property rights were rudimentarily defined by the hierarchical organizational structure, rather than the reverse.

In the standard principal-agent model described above, asymmetric property rights define the authority relationship between the two parties: principals can give orders because they own the assets in question. This authority asymmetry balances the information asymmetry favoring agents and permits the hierarchy to function predictably. In a Soviet-type system, by contrast, the authority of the principal to command the agent can be confirmed only by the agent's willingness to accept that authority. Insubordinate agents could, of course, be removed by force, but most cases of insubordination failed to warrant such an extreme response. Absent specific countermeasures from superiors, agents could easily begin to use the powers delegated to them *as if* they were their own. Thus, in most hierarchical settings within the Soviet system, we might well regard property rights as having been indeterminate.

## AUTHORITY

As I have already noted, all hierarchical systems are authority structures. Holmstrom and Tirole observed that "the rights of authority at the firm level are defined by ownership of assets, tangible (machines or money) or intangible (goodwill or reputation)."[18] The preceding discussion has suggested, however, that in Soviet organizations the principle of ownership flowed from the demonstration of authority. How can this circularity be resolved?

Returning to the two-actor principal-agent model, it is somewhat easier to visualize authority as a consensual relationship. To say the principal has authority is to acknowledge that the agent accepts her power to issue orders—at least over a range of activities defined as the agent's "zone of acceptance."[19] This acceptance may be based upon the explicit recognition of the principal's claim of property ownership (that

[17] A parallel argument in which property rights are derived from de facto control over assets, rather than vice versa, is developed in John Umbeck, "Might Makes Rights: A Theory of the Formation and Initial Distribution of Property Rights," *Economic Inquiry* 19, no. 1 (1981). Umbeck considers property rights in weakly organized environments, but not within organizations.

[18] Bengt R. Holmstrom and Jean Tirole, "The Theory of the Firm," in Richard Schmalensee and Robert Willig, eds., *Handbook of Industrial Organization* (Amsterdam: Elsevier, 1989), 123.

[19] The notion of "zone of acceptance" can be traced back to Chester Barnard, *The Functions of the Executive* (Cambridge: Harvard University Press, 1938). Barnard initially referred to a "zone of indifference," but the concept was reformulated and relabeled by Herbert Simon. It can be thought of as that range of actions covered by the employment contract between principal and agent. On the zones of acceptance and neoinstitutional analysis, see Oliver Williamson, "Chester Barnard and the Incipient Science of Organization," in Williamson, ed., *Organization Theory: From Chester Barnard to the Present and Beyond* (New York: Oxford University Press, 1990), esp. 175–76.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

is, the understanding that this claim would be supported by a court or arbitrator), or it may be based on the assumption that the principal could, if necessary, force the agent to obey. The latter situation prevailed in the Soviet case, and the former (the confirmation of asset ownership) emerged as a consequence. In turn, the principal's power derived from her position in the hierarchy, which had been unchallenged since Stalin. As Arrow has noted, "When conditions are stable, the role of authority . . . is taken for granted and is little questioned."[20]

Public bureaucracies differ from private organizations, however: they control the vast resources of the state, including its instruments of coercion. As Moe has discussed, principals' "property rights" are uncertain for politicians or political appointees even in democratic systems, since they face the prospect of losing power at each election.[21] At the same time, actors in any public bureaucracy may receive delegated power that is binding even over their principals. Thus, attorneys general may investigate presidents or congressmen, and KGB officers may undermine Party bosses.[22]

Authority relations, like property rights, cannot be taken for granted in a principal-agent framework. I have argued that authority claims and property claims (including rights of control over such political assets as personnel appointments or media access) are closely linked in this model of hierarchy, where agents' acceptance of authority implies an acceptance of principals' "ownership." This is especially important in systems like the Soviet bureaucracy, which lacked an authoritative third-party adjudicator of conflicting property claims. In Williamson's words, "Hierarchy is its own court of ultimate appeal."[23] In many cases, however, possession is nine-tenths of the law.

## RISK SHARING

Application of principal-agent models to public bureaucracies also demands a reexamination of some of its assumptions concerning risk sharing. In the standard model of the agency contract, the agent ex-

[20] Arrow (fn. 16), 64.

[21] Terry Moe, "Political Institutions: The Neglected Side of the Story," *Journal of Law, Economics and Organization* 6-S (1990).

[22] Phil Roeder has proposed a model of "bureaucratic reciprocal accountability" to capture the phenomenon of appointed officials gaining power over the "selectorate" that appointed them; see Roeder, *Red Sunset* (Princeton: Princeton University Press, 1993). As Moe and others have discussed, however, it is not only in authoritarian systems that agents gain power over the principals who appointed them. Roeder's model does not explain how reciprocal accountability is transformed into hierarchical accountability or how either is enforced below the Central Committee level.

[23] Oliver E. Williamson, "Comparative Economic Organization: The Analysis of Discrete Structural Alternatives," *Administrative Science Quarterly* 36 (June 1991), 274.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

changes uncertainty over her compensation in return for making the principal the residual claimant to output from her labors.[24]

However, in a public bureaucracy there is no residual. Furthermore, bureaucracies in command economies generally faced soft budget constraints: the state covered their operating losses.[25] Taken together, these observations imply that principals in a Soviet-type hierarchy were neither profit maximizing nor budget balancing.

An important consequence of this abrogation of managerial discipline is the nullification of almost all downside risk for principals.[26] Standard agency theory assumes that their claim to the residual gives principals a real stake in uncovering agents' hidden information. This assumption must be questioned for Soviet-type systems.

If principals are—or even if they believe themselves to be—insured against the risk of plan failure, they may have few incentives to aggressively develop better solutions to hidden information problems. Even at the top of the hierarchy, officials' real self-interest may frequently lie, not in maximizing output, but rather in preserving their privileged positions by simply appearing to maximize output.

These deviations from the standard assumptions of agency models begin to define a more explicitly political variant of the principal-agent relationship, in which environmental characteristics like property rights, authority claims, and risk sharing are more subtly interrelated.[27] They also set the stage for considering how the stable relationship of delegated authority depicted by the standard agency model can unravel until the principal no longer controls the agent. This process might be triggered by changes in either contract mechanisms or the contracting environment.

## II. Explaining Institutional Change

In the principal-agent model of Soviet-type bureaucracies discussed above, principals' property rights over both (tangible and intangible)

[24] Bengt Holmstrom, "Moral Hazard and Observability," *Bell Journal of Economics* 10, no. 1 (1979); Holmstrom and Tirole (fn. 18), 88–92.

[25] The term was introduced by Kornai in 1980 and is summarized in Kornai (fn. 4), 140–45.

[26] Winiecki makes a similar point by arguing that the Soviet system protected the rents of key officials and industrial managers from any consequences of their job performance. See Jan Winiecki, *Resistance to Change in the Soviet Economic System: A Property Rights Approach* (London: Routledge, 1991).

[27] These characteristics are not exclusive to Soviet-type systems. Highly decentralized or dispersed nonmarket hierarchies like empires, public schools, or even the medieval Catholic church may display some similar characteristics. Though beyond the scope of this article, the model of disintegration described in the next section may also be useful in explaining organizational decay in these systems.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

could be understood as ambiguous but unchallenged. They depended fundamentally upon agents continuing to abide by the agency contract and manage institutional assets in the principal's interests, rather than in those of the agent. If one agent was revealed to be in violation of this contract and the principal was unable to remove those assets from her control, we might reasonably conclude that the principal no longer really "owned" the assets in question. The agent's behavior would have gone from shirking to outright appropriation. We might conclude that the principal could no longer exercise her authority over that agent to enforce their contractual arrangement, and other agents under contract to that principal might draw similar conclusions.

The process I am describing is in many ways the inverse of a bank run. A bank might be thought of as a single agent with multiple principals. When I place my money in a bank, I retain ownership but temporarily delegate control over those assets to the bankers. If I learn that another investor has been denied access to her account—or even if I believe this is about to happen—this reveals for me some hidden information about the health of the bank. I rush to reclaim my assets, but so does everybody else. The bank fails, leaving all investors poorer, even though the bank might have survived had we not all panicked.

Now consider the inverse case: I am one of several agents managing different shares of a single principal's assets (call him Andrei). Facing hidden action and hidden information problems, Andrei has designated specific performance targets for us to meet; as long as I successfully meet these targets (or at least convince Andrei that I have met them), my use of my share of his assets is largely unmonitored. I may choose simply to use Andrei's assets to employ my friends and to rob a bank monthly to meet my target, keeping the surplus and including a fictitious report of virtuous investments to keep Andrei happy.

If I now learn that a second agent—call her Zena—has stolen Andrei's money without any reprisals, I face a dilemma. If Andrei goes bankrupt—and Zena's defection has certainly weakened him—all agents will probably lose their access to Andrei's resources. From my perspective, his property rights are suddenly uncertain, making my delegated rights even more precarious. If I defect, Andrei's demise becomes more likely, but I will at least secure control of whatever assets I manage to take with me.[28] Facing this one-shot, n-person Prisoner's Dilemma, my defection is extremely likely. Following the logic of the

[28] Presumably some intangible assets, like reputation, will not be transferable.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

bank run, I rush to claim my assets before it is too late, even though the assets really belong to Andrei.[29]

What in practice might trigger the sudden erosion of principals' authority and begin this organizational breakdown? The critical element in this process is the *perception* that the principal can no longer control his resources. This perception could result from several developments; for the purposes of this analysis, I will consider situations in which agents begin to exercise greater autonomy from principals.[30]

Greater autonomy for agents can result from less rigorous monitoring or more flexible performance targets. Either of these modifications to the basic agency contract could be introduced by a principal (perhaps newly selected) who set out to motivate agents to improve real, rather than reported outcomes. In both the Soviet Union and China, for instance, fiscal reforms that granted local officials limited discretionary control over their budgets had this initial goal.

Offering greater autonomy to agents, however, assumes that agents have up to that point been operating well within the zone of acceptance recognized by both principal and agent. The motivation for reform, in other words, is the presumption that the plan dictated by the principal has been too restrictive. In the situation presented here agents have already narrowed this zone of acceptance considerably, because the fundamental problems of information asymmetry were never adequately resolved. As noted in the previous section, once plan targets were met, agents would divert inputs to building up a safety margin. Additional resources, combined with this accumulated safety margin, could give agents the capacity to resist further exercise of authority from the center. Once all parties recognize this, a process of disintegration is unleashed.

A comparable result emerges from considering similar reforms within the game-theoretic model of organizations as repeated short-

[29] Nee and Lian (fn. 3) develop a similar scenario, based upon Granovetter's "threshold" model of collective behavior. According to their analysis, the likelihood of a Communist Party activist becoming an opportunist and defecting from the organization is strongly related to the extent of opportunism among other Party activists. They attribute this to the "demonstration effect" that spreads opportunism from higher ranking officials through the organization. In the model developed here, the observable opportunism of other agents may also provide still-loyal actors with new information about the viability of the parent organization and thus about the likelihood of receiving the "sucker's payoff" in the event of organizational collapse. This signaling effect of protest or defection—as distinct from more straightforward demonstration effects—is described for the phenomenon of mass protest in Susanne Lohmann, "Dynamics of Informational Cascades: The Monday Demonstrations in Leipzig, East Germany, 1989-91," *World Politics* 47 (October 1994).

[30] An alternative scenario could be the emergence of alternative or competing principals. For a general analysis of this phenomenon, see David Epstein and Sharyn O'Halloran, "The Multiple Principals Problem in Politics," Political Economy Working Paper (New York: Columbia University, 1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

term agency contracts. As I noted earlier, the iterated nature of the contracting game reduces the opportunity for agents' shirking, provided (1) the relationship is open-ended or the future is not highly discounted, and (2) agents have limited access to outside credit. The shifts described above undermine precisely these conditions: uncertainty over principals' property rights can cast doubt over the future of the agency relationship and encourage a greater emphasis on near-term payoffs. Greater discretionary control over assets can effectively weaken agents' credit dependence on their superiors. Put more starkly, if employees suspect their boss might soon be replaced and they can afford to lose a bonus or two, the temptation to cheat or even steal will rise dramatically.

## III. Strategies for Arresting Collapse

The preceding account of the organizational bank run describes incentives and choices largely from the perspective of the multiple agents who begin to sense that their principal may be weakening. In this section, I briefly consider the principal's perspective.

Consider the situation in which multiple agents contract with a principal under conditions of imperfect information.[31] If the future is discounted or the contract period is finite, the principal must weigh the costs of ignoring individual challenges to his authority (assuming retaliation is costly) against the costs of retaliating forcefully against all challenges to establish his reputation and discourage future challenges.

Analyses of reputational effects have often built upon the model of a chain-store game, in which a monopolist faces potential competitors in a series of discrete markets.[32] The overriding lesson of the chain-store game is that the long-term player (the monopolist) may choose to sacrifice short-term gains to build up a reputation that will deter some or all future competitors. In other words, he can try to convince risk-averse competitors that he is temperamentally aggressive and will therefore incur the costs of challenging any and all competitors. Absent this reputational effect, regional challengers playing a game in which

[31] This discussion draws on David M. Kreps, "Corporate Culture and Economic Theory," in James E. Alt and Kenneth A. Shepsle, eds., *Perspectives on Positive Political Economy* (Cambridge: Cambridge University Press, 1990), esp. 100–116.

[32] See Reinhard Selten, "The Chain Store Paradox," *Theory and Decision* 9 (April 1978), as well as the subsequent discussions in David Kreps and Robert Wilson, "Reputations and Imperfect Information," *Journal of Economic Theory* 27 (August 1982); and Paul Milgrom and John Roberts, "Predation and Entry Deterrence," *Journal of Economic Theory* 27 (August 1982).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

the future is discounted will expect the monopolist to shift eventually to an end-game strategy and begin acquiescing to limit his losses.[33]

Consider now a variation on the chain-store game in which a single principal controls a large number of agents operating in different regions. In each period another agent must decide whether to challenge the authority of the principal and appropriate his assets. (This is analogous to saying that the challenge to the monopolist comes not from regional competitors but from his own branch managers, each of whom is considering setting up his own shop and stealing the monopolists' local operating payroll, customer list, employees, and so on.) Information flows are highly imperfect: the agent's decision may not be immediately apparent to the principal, nor may the principal's response be unambiguously understood by other agents. Agents with a large accumulated surplus will not be deterred from defecting, because they feel they are already beyond the reach of the principal. The question for the principal then is how best to minimize defections among other agents.

As I have already implied in discussing the bank run scenario, agents will look at the exchanges between the principal and other agents to assess the likelihood of succeeding at defection. Given the noisiness of the information environment, principals will need to respond to challenges quickly and forcefully to establish their reputation for retaliation. Furthermore, they should probably choose weaker agents for retaliation, since a failed retaliation will lead to an even more rapid erosion of reputation and, by extension, authority.

In the postwar Soviet case the rare challenges to the authority of the leadership were met quickly with a coercive reply. From this perspective, the fixation of the Western media during the 1970s and 1980s on the anemic dissident movement within Russia may have had a mixed effect. Whereas it publicized the existence of dissent, it also amplified the regime's harsh response to this limited challenge. By reporting on this response through authoritative foreign broadcast channels, Western media probably enhanced the regime's domestic reputation for punishing nonconformity.

Such shows of force were inappropriate within structures of state

[33] The discussion of reputation effects in this section draws on the discussions in Drew Fudenberg and Jean Tirole, *Game Theory* (Cambridge: MIT Press, 1991), chap. 9; and David M. Kreps, *Game Theory and Economic Modelling* (Oxford: Oxford University Press, 1990), 65–72. See also Drew Fudenberg and David K. Levine, "Maintaining a Reputation When Strategies Are Imperfectly Observed," *Review of Economic Studies* 59 (July 1992); and James E. Alt, Randall L. Calvert, and Brian D. Humes, "Reputation and Hegemonic Stability: A Game-Theoretic Analysis," *American Political Science Review* 82 (June 1988).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

power, however, at least in the post-Stalin era.[34] Corruption by officials was rampant under Brezhnev, and the anticorruption drives of Andropov and Gorbachev were limited in scope. Thus, when local officials began blatantly appropriating the assets of state organizations, few alternatives other than dismissal were available to supervisors. As I discuss below, even dismissal became an empty threat when the assets removed from these organizations were sufficient to underwrite more lucrative future employment.

## IV. Applying the Model: Consequences of Devolution in the Soviet Union and China

The preceding analysis highlighted five key factors that could cause a limited devolution of decision-making authority to produce a collapse of organizational structure.

1. If devolution of control rights over organizational assets exacerbates information asymmetries between principals and agents (for instance, by weakening monitoring mechanisms), opportunism by agents becomes far more likely.
2. If agents had previously been operating opportunistically and had accumulated significant safety margins (in response, for instance, to pervasive ratcheting), devolution of additional control rights could permit them to expropriate organizational assets altogether.
3. Given the ambiguity of property rights within organizational hierarchies, loss of control over certain assets may undermine principals' authority to enforce other property rights claims without resorting to force. Consequently, other agents may reassess either the risks of their own opportunism or the risks of remaining loyal to a weakened organization.
4. If principals are shielded from the consequences of misappropriation of their assets, they will lack the proper incentives to police their agents.
5. If principals wish to restore their reputations and check the erosion of their authority, they must move quickly and unambiguously to discipline opportunistic agents and to clarify the distribution of property rights.

To evaluate these assertions, I briefly review the processes that unfolded in the Soviet Union and China, as authorities in Moscow and Beijing attempted limited decentralizing reforms. This comparison of complex systems is intended to be suggestive rather than rigorous. By examining the incentives faced by individual actors in parallel economic, political, and state fiscal hierarchies, I seek to demonstrate that

[34] Peter Hauslohner, for instance, considered the virtual elimination of the use of violence against members of the ruling elite to be one of the defining "rules" of post-Stalin politics. See Hauslohner, "Politics before Gorbachev: De-Stalinization and the Roots of Reform," in Seweryn Bialer, ed., *Politics, Society and Nationality inside Gorbachev's Russia* (Boulder, Colo.: Westview Press, 1989), esp. 44–48.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

the model outlined above offers insight into the different paths taken by the institutions themselves.

## Soviet Reforms, 1985–91

The earliest organizational reforms in the Gorbachev period affected the economy and were intended to transfer decision-making power from central planners to firm-level managers, in part to alleviate problems of hidden information.[35] The 1987 Law on State Enterprises began the shift from mandatory central planning to a less comprehensive system of state orders, by introducing self-financing for firms and other organizational units. Subsequent legislation provided for the establishment of cooperatives or "small firms" that operated under the umbrella of larger state enterprises but that were organizationally and legally distinct. In theory, these moves implied that the budget constraints faced by managers would become harder, but that they would also have more options available (for example, sale of some proportion of their output at liberalized prices) to respond to these new incentives.

In practice, however, the reduced role of the State Planning Agency (Gosplan) translated into a sharply reduced capacity for monitoring agents' activities at all levels of the centrally planned hierarchy, since the planning system acted simultaneously as the state's management information system.[36] Consequently, the cooperatives and small enterprises established by firm managers enabled them to remobilize many assets of state enterprises into organizational units less clearly owned by state ministries.

These microlevel realignments came to be known as "spontaneous privatization," since a frequent pattern was the de facto expropriation by managers and ministerial bureaucrats of many assets belonging to state enterprises.[37] In many cases these spontaneously privatized concerns collaborated with state bureaucrats eager to "privatize" the functions of the ministries themselves. In the brief period from 1989 to 1991 many managerial responsibilities previously discharged by the in-

[35] For standard accounts of the early Gorbachev reforms, see Hewett (fn. 4); Anders Åslund, *Gorbachev's Struggle for Economic Reform* (Ithaca, N.Y.: Cornell University Press, 1989); and Ed Hewett and Victor Winston, eds., *Milestones in Glasnost and Perestroika*, vol. 2, *The Economy* (Washington, D.C.: Brookings Institution, 1991).

[36] As Eugène Zaleski has written, "It seems more nearly correct to call the [Soviet] economy 'centrally managed' rather than centrally planned." See Zaleski, *Stalinist Planning for Economic Growth* (Chapel Hill: University of North Carolina Press, 1980), 484.

[37] Simon Johnson and Heidi Kroll, "Managerial Strategies for Spontaneous Privatization," *Soviet Economy* 7, no. 2 (1991). The process was also observed and documented in East Central Europe (particularly Poland and Hungary), where the obvious economic advantages it accorded the political ruling class earned it the label "nomenklatura privatization."

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

dustrial planning hierarchy were internalized by enterprises themselves or shared with horizontally or vertically integrated *kontserny*.[38] Even in those cases where *kontserny* duplicated many of the functions of ministries, their creation served the same function as more radical forms of enterprise-level privatization: the property rights of state actors at higher levels of the bureaucracy over firm-level assets were either blurred or abrogated altogether.

Once it became clear that the ministerial supervisors were unable (or unwilling, given the rent-seeking potential) to stop enterprise managers from claiming de facto ownership rights over assets, the pace of spontaneous privatization accelerated. New "commercial banks" (themselves the result of spontaneous privatization within state banks) became active financiers of managerial buyouts.[39] Industrial ministries consequently disintegrated well before the 1992 initiation of a formal privatization program in Russia. Once privatization was decreed, managers extracted important policy concessions to protect their newly won control over enterprise assets; in other words, the property rights they grabbed in 1989-91 during the enterprise-level bank run proved remarkably durable.[40]

While the hierarchical links within the branch ministries were disintegrating, a similar process was unfolding within the federal and regional administrative systems of the Soviet state. In 1989 the Soviet government began a restricted initiative to devolve certain functions from Moscow to regional levels, reducing direct transfers from the center while giving regional governments new taxing authority over local enterprises.[41] In short order, subnational budgets came under severe pressure from declining tax revenues (the new Law on State Enterprises essentially wiped out the profits that were to be taxed by regional

[38] Johnson and Kroll (fn. 37). See also Stephen Fortescue, "The Restructuring of Soviet Industrial Ministries since 1985," in Anders Åslund, ed., *Market Socialism or the Restoration of Capitalism* (New York: Cambridge University Press, 1992). The neologism *kontserny*, from the English "concerns," translates roughly as "conglomerates."

[39] On the role of new banks, see Joel Hellman, "Breaking the Bank: Building Market Institutions in the Former Soviet Union" (Ph.D. diss., Columbia University, 1993); and Juliet Ellen Johnson, "The Russian Banking System: Institutional Responses to the Market Transition," *Europe Asia Studies* 46, no. 6 (1994).

[40] These policy concessions by Russian policymakers, consisting chiefly of expanded opportunities for management buyouts of privatizing firms, are described in Michael McFaul, "State Power, Institutional Change, and the Politics of Privatization in Russia," *World Politics* 47 (January 1995); and Maxim Boycko and Andrei Shleifer, "The Politics of Russian Privatization," in Olivier Blanchard et al., *Post-Communist Reform: Pain and Progress* (Cambridge: MIT Press, 1993).

[41] Donna Bahry, "The Union Republics and Contradictions in Gorbachev's Economic Reform," *Soviet Economy* 7, no. 3 (1991).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

governments) and reduced subsidies from the center.[42] Consequently, regional officials began seeking new sources of revenue, ranging from ad hoc taxes and fees to joint ventures. Since it was virtually impossible for Moscow to measure the scope of these extrabudgetary revenue flows accurately, the activity of regional officials became more difficult to monitor and control through the standard planning mechanisms of the budget.

As regional and republican governments concentrated on closing their own fiscal gaps and on providing new services to voters in upcoming regional elections, they also began selective withholding of revenue transfers from Moscow. Moscow's response to these trends shows a lack of clear resolve. In late 1989, for instance, the Baltic republics lobbied for and received a special economic status that allowed them to define their own tax and fiscal systems. During 1990, however, the Soviet government moved to restrict their autonomy sharply: Lithuania was blockaded, and Estonia was ultimately forced to forward tax payments it had been withholding.

After Yeltsin's election in the summer of 1990 and the subsequent declaration of "economic sovereignty" for the Russian Federation, it became impossible for Soviet leaders to maintain the charade of control over republic-level finances. Yeltsin had the capacity to implement a single-channel tax payment system for Russia unilaterally; other union republics sensed the vulnerability of the Soviet government and quickly followed suit. Coupled with unorthodox regional-level revenue-generating schemes that were difficult to monitor, Soviet leaders found it impossible even to draw up a consolidated budget for 1991.[43] The center found its traditional revenue sources suddenly choked off. Gorbachev could do little to recapture fiscal resources seized by subnational officials except plead for a substantial role for Moscow in the planned federation treaty. Thus, the bank run by regional officials was essentially irreversible by early 1991, almost a full year before the formal disintegration of the Soviet Union.

Disintegration of both industrial and federal hierarchies within the Soviet system should have been contained by the unitary political structures extending from the Kremlin to every factory and every level of government. The Communist Party—and related "transmission belts"

[42] Daniel Berkowitz and Beth Mitchneck, "Fiscal Decentralization in the Soviet Economy," *Comparative Economic Systems* 34 (Summer 1992).

[43] Bahry (fn. 41), 247; Berkowitz and Mitchneck (fn. 42), 2. A budget for 1991 was eventually approved but rendered moot after revenue projections proved meaningless; see John Tedstrom, "Soviet Fiscal Federalism in a Time of Crisis," *Report on the USSR* 3, no. 31 (1991).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

like the Young Communist League (Komsomol) and trade unions—were explicitly created as monitoring organizations to preserve hierarchical authority throughout Soviet society. However, opportunism by local agents within these political structures produced an organizational bank run that magnified the centrifugal tendencies in state and federal hierarchies.

The chaos surrounding the collapse of the Communist Party in August 1991 has made it unlikely that we will ever be able to fully document internal Party financing or the behavior of local officials during the Party's final years. Extensive evidence is available, however, on internal dynamics of the Komsomol, which embarked on similar reforms several years ahead of the Party. The Komsomol copied the CPSU's structure, with primary organizations operating in schools, army units, and workplaces, and the hierarchy reached up through district, regional, and republican committees to the Central Committee in Moscow.[44] Like the Party, it controlled not simply a mass membership but also an extensive network of real estate, publishing houses, travel companies, and liquid assets (in both dollars and rubles). It therefore serves as a useful proxy for the Party.

Party leaders entrusted the Komsomol with the intangible job of indoctrination, and Komsomol officials interpreted this to justify a broad range of actions. Success in indoctrination was difficult to assess, so supervisors at each level of Komsomol's hierarchy were obliged to set concrete performance targets in order to exercise control over their subordinates. The targets that received the greatest attention were those dictating annual enrollments of new members. Each year, the target for membership saturation (that is, the percentage of Komsomol-age youth enrolled in the league) was ratcheted up slightly.

Within the organization subordinates at each rung of the ladder down to street-level primary organizations could exercise considerable latitude in deciding how to meet these performance targets. Many chose to force enrollment with little attention to ideological training, while others found it simpler just to falsify statistics. In either case, their control over the flow of information up the bureaucratic hierarchy al-

[44] Some useful sources on the history of the Komsomol include Allen Kassof, *The Soviet Youth Program* (Cambridge: Harvard University Press, 1965); Peter Kenez, *The Birth of the Propaganda State* (Cambridge: Cambridge University Press, 1985); and Jim Riordan, "The Komsomol," in Riordan, ed., *Soviet Youth Culture* (Bloomington: Indiana University Press, 1989). For an account of Komsomol under Brezhnev and Gorbachev, based in part on documents from the Komsomol archives, see Steven Solnick, "Growing Pains: Youth Policies and Institutional Change in the Former Soviet Union" (Ph.D. diss., Harvard University, 1993), 103–218.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

lowed them to appear to meet their objectives from year to year, thus ratifying and perpetuating the bureaucratic chain of command.

In the 1980s demographic shifts made it impossible for local officials to continue concealing the hidden actions that facilitated plan compliance. A contraction in the target age cohort of fourteen to twenty-eight year olds coincided with overall membership saturation in excess of 65 percent. This forced local officials to engage in ever more blatant ploys to sweep every fourteen year old into the league—and to continue counting long-departed members—to reach enrollment targets.[45] Enrollment meetings became farces in which sullen candidates were automatically sworn in and forced to hand over their dues. In 1984 the widespread cynicism of Komsomol officials was lampooned in a popular novella that was later made into a hit film.[46]

In the context of this growing crisis in public esteem, Moscow's limited reforms beginning in 1986 (which foreshadowed the enterprise and federal reforms described above) could have been viewed as a reasonable strategy for revival. Binding membership targets were replaced by a fiscal incentive: local budgets would be based directly on dues. These budgets would then be placed under the direct control of local committees so that new programs tailored to local needs could be quickly adapted to the interests of potential new members.[47] However, when Komsomol officials abandoned budgetary control and membership targets, they also dismantled the primary information channels of their system of hierarchical administration. Administrators in Moscow, or even in regional capitals, had no direct way of monitoring the activities of local officials.

Freed from central control, local officials abandoned most efforts at enrolling new members. Komsomol's assets were far more important than dues, especially in the Wild West economic environment of 1987.

[45] By 1984 over half of all new members joining the Komsomol were fourteen year olds; VLKSM: *Nagliadoe posobie po komsomol'skomu stroitelstvu* (Moscow: Molodai gvardiia, 1985). Enrollment practices of local Komsomol organizations were criticized in a Communist Party resolution published in *Pravda*, July 7, 1984.

[46] Iurii Poliakov, "ChP raionnogo masshtaba," *Iunost'*, no. 1 (1985), 12–50. In the wake of the publication of this work and later the release of the film, public criticism of Komsomol poured into the press. For a typical sample of letters from disgruntled members, see *Sobesednik*, no. 38 (1986), 4–5.

[47] The abandonment of membership targets was announced by the new first secretary of Komsomol, Viktor Mironenko, in August 1986; reprinted in Mironenko, *Pis'mo s"ezdu* (Moscow: VLKSM, 1987). The new fiscal policies were announced at the Komsomol's Twentieth Congress, held in April 1987. They were initially introduced as a limited experiment in fifty-six large primary organizations but were then extended throughout the organization over the next two years. By 1989 the budgetary and financial operations of each level of the Komsomol hierarchy were almost completely isolated. The reforms are reviewed in *Komsomol i molodezh' Rossii (Delegatu s"ezda komsomol'skikh organizatsii RSFSR)* (Moscow, 1990) (Brochure distributed to delegates at the first Conference of Komsomol Organizations of the Russian Federation).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Perceiving signs of weakness at the center, local agents rushed to appropriate those assets over which their committees could assert control. Local officials took advantage of the new laws on cooperatives to open travel agencies, cafés, and video salons on Komsomol property; they even used money from Komsomol accounts to invest in the first wave of new commercial banks.[48] The bank run that emptied Komsomol's coffers was very real, except the funds withdrawn had come from the dues of other, rank-and-file depositors, accumulated over several decades.

Once officials on the Komsomol Central Committee began to receive clear signals that local and regional organizations were slipping out from under their control—and republican committees in the Baltics and Caucasus began moving openly to secede from the Komsomol—they took no overt action to bring these renegade officials under control. Instead, they began shifting the assets of the Central Committee itself into commercial ventures, to deny defecting committees any share of these resources.[49] The most blatant move came in 1988, when the Komsomol Central Committee established the Commercial Youth Bank with a starting fund of 250 million rubles taken from Central Committee accounts; an additional 500 million rubles was transferred to this bank by 1990.[50]

Thus, officials in regional and local committees took advantage of their newly granted autonomy from the center to develop alternative sources of income and, ultimately, employment. When central authorities began to shield their assets, they signaled that they were preparing for possible organizational fragmentation and probably lost the chance to recover their reputation for punishing challengers. Faced with these signals, local officials continued the de facto privatization of assets at their level, and the hierarchical structure imploded.

By the time of the August 1991 coup, Central Committee staffers and local committees had in effect already plundered and divided the

[48] For typical accounts, see I. Larin, "Komsomol on the Verge of Change," *Argumenty i fakty*, no. 12 (1987); and David Remnick, "Brash New Breed 'Building Empires, Not Evil Ones,'" *Washington Post*, July 7, 1991, p. 1.

[49] These maneuvers were revealed by Viktor Graivoronskii, a Moscow Komsomol official, in *Moskovskii komsomolets*, April 24, 1990.

[50] There can be little doubt that these moves were efforts to shield the center's assets from the forces of disintegration. Then first secretary of the Komsomol, Viktor Mironenko, asserted that no republican Komsomol committee that seceded from the organization could claim a share of any Central Committee investments in banks or stock-holding companies. (Interview with author, Moscow, March 20, 1991). At the time of this interview, the question was already far from academic, since several of these ventures (like Menatep) had become commercial giants, and the Lithuanian and Estonian Komsomol organizations had either shut down or broken away from Moscow.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Komsomol's chief assets. Central Committee members debated how best to restructure its leading organs "so that only those who can make money can continue in office."[51] In September 1991 the Komsomol convened one last congress to divide up its remaining assets. Participants were chiefly concerned with defining the property rights of the organization's twenty-three successor committees.

As I have already suggested, the collapse of the CPSU followed the Komsomol's pattern closely, but began later and was interrupted by the August coup. Beginning in 1987 and accelerating after the Nineteenth Party Conference in 1988, local and regional Party posts began to be filled by competitive elections. Carried to its logical extreme, this practice implied that principals within the Party hierarchy could no longer summarily replace insubordinate agents, if those agents owed their position to direct elections. It also changed agents' incentives, introducing a new degree of uncertainty about their tenure, since not all risk could be transferred to their principals.[52]

Regional and local Party officials were also granted greater authority over their own budgets, a process stressed at the 1990 Party Congress. However, this devolution of power from the Kremlin was a mixed blessing at best. Declining profitability of the Party's economic activities (particularly publishing) coupled with the unprecedented drop in Party membership (down approximately 20 percent in the eighteen months after January 1, 1990) created severe budget gaps at all levels of the Party hierarchy.[53] As Komsomol officials had already learned, transferring responsibility for budgets in this environment was equivalent to transferring responsibility for deficits. Local Party officials quickly discovered it was simpler—and less uncertain—to seek new revenue sources through commercial activity than through recruiting new members. And with levers of monitoring and sanctioning weakened, officials in Moscow could do little to guarantee that the profits of these activities remained in Party coffers.

Beginning around the Twenty-eighth Party Congress in 1990, regional Party officials began preparing their "golden parachutes"—using Party funds to set up regional banks and enterprises where many would

[51] *Nezavisimaia gazeta*, September 7, 1991, p. 2.

[52] This practice was also introduced in the Komsomol, but only after the bank run had already been triggered by internal fiscal reforms. Komsomol officials also faced a natural term limit in the form of age ceilings for most officials, so the impact of elections on incentives was less severe.

[53] The budgetary problems of the Party are reviewed in *Izvestiia TsK KPSS*, no. 8 (1990), 91–98. On budgets and also membership, see Elizabeth Teague and Vera Tolz, "CPSU R.I.P.," *Report on the USSR* 3, no. 47 (1991); and Stephen White, Graeme Gill, and Darrell Slider, *The Politics of Transition: Shaping a Post-Soviet Future* (New York: Cambridge University Press, 1993), 117–39.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

find employment after the August 1991 coup. In June 1991 the Politburo approved the transfer of 600 million rubles of central Party funds to commercial organizations (including those created earlier by the Komsomol and through spontaneous privatization of enterprises), thus insulating these funds from the consequences of the Party's impending disintegration. This action certainly signaled uncertainty in the minds of Party leaders over the fate of the Party, and helped accelerate the bank run. At the time of the August coup Party property at all levels was being transferred to "private" owners, in a systematic effort to keep these assets under nomenklatura control.[54]

## Organizational Survival: Chinese Reforms, 1979–94

In China, beginning in 1979, reforms also devolved property rights over many industrial assets and regional fiscal resources from central leaders to lower-level officials.[55] As in the Soviet Union, these reforms gave agents at lower levels of the political and economic hierarchies the opportunity and capability to defy principals' authority and break hierarchical controls. In China, however, these controls have strained but not snapped. Though China watchers have begun to ask whether the center can hold,[56] to a Soviet watcher the remarkable feature of Chinese reforms is that the center has held even this long.

In the early 1980s economic reforms in China transferred significant autonomy to local and regional governments in two ways. First, in a process akin to spontaneous privatization, local authorities were granted extensive property rights over economic enterprises under their jurisdiction, triggering an explosion of so-called town and village enterprises (TVEs). Second, in a shift analogous to Soviet fiscal decentralization, local regions were entitled to keep a significant share of the

[54] The story of the Party's massive "ruble launderette," based on documents from the Central Committee archives, is described in Stephen Handelman, *Comrade Criminal* (New Haven: Yale University Press, 1995), 93–114. Although these documents cover the Party's efforts to shield Central Committee funds, the fate of regional Party assets may never be known. The Party's treasurer, Nikolai Kruchina, committed suicide in the wake of the August 1991 coup.

[55] The literature on Chinese reform is vast. In addition to accounts cited in fn. 1 and specific citations in the text, I have also drawn more generally on Susan L. Shirk, *The Political Logic of Economic Reform in China* (Berkeley: University of California Press, 1993); Gordon White, *Riding the Tiger: The Politics of Economic Reform in Post-Mao China* (Stanford, Calif.: Stanford University Press, 1993); Jia Hao and Lin Zhimin, eds., *Changing Central-Local Relations in China: Reform and State Capacity* (Boulder, Colo.: Westview Press, 1994); and Victor Nee, "Organizational Dynamics of Market Transition: Hybrid Forms, Property Rights and Mixed Economy in China," *Administrative Science Quarterly* 37 (March 1992).

[56] "Can the Centre Hold?" *Economist*, November 6, 1993, p. 32. See also the review of recent debates by David S. G. Goodman, "The Politics of Regionalism," in David S. G. Goodman and Gerald Segal, *China Deconstructs* (New York: Routledge, 1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

taxes on regionally "owned" enterprises, passing only a negotiated percentage on to the central government. In many regions local officials were rapidly transformed into rich industrialists, who operated with great independence from those above them in the hierarchy.

By the late 1980s, however, the economy in several regions was in danger of severely overheating. Officials at the center attempted to slow economic growth, which in practice meant slowing growth in precisely those regions whose economic success had made them most independent of Beijing. The retrenchment of 1988–91, though imperfectly administered, did succeed in moderating the overall growth rate and driving out the most dangerous inflationary threats.

Since then, however, control over regional officials has been incomplete. Certain regions successfully resisted the imposition of a unified tax code and evaded attempts to limit investment levels in overheated regions.[57] Furthermore, at its landmark November 1993 plenum, the Chinese Communist Party leadership agreed to moderate its five-month austerity drive in order to win regional acquiescence in its plans to restructure the banking and fiscal systems.[58]

By contrast with the Soviet experience, the striking question for China is how officials in Beijing managed to maintain any measure of control over thriving local economies in the face of reforms that gave local officials access to resources not directly administered by the center. In Russia, as discussed above, external resource flows acquired by agents in economic, state, and political hierarchies made it possible for them to defy hierarchical authority—a situation that triggered structural disintegration. In China, although local officials had some success in resisting the intervention of the center, their resistance never triggered the sort of bank run that would render impossible any assertion of authority by leaders in Beijing. How did the Chinese leadership preserve its influence over its local agents as it presided over a reform whose hallmark was devolution of power to regional administrators?

Several mutually reinforcing explanations are possible. First, while the Chinese Communist Party gained new revenue sources from the regional growth explosion, the Party itself avoided internal restructuring along the lines of the CPSU. Second, Chinese reforms clarified rather than obscured property rights, and created incentives that addressed rather than exacerbated problems of hidden action and hidden information. Finally, Chinese leaders were more prepared to take deci-

[57] See, for instance, Shirk (fn. 55), 175; and "Can the Centre Hold?" (fn. 56).

[58] Dali L. Yang, "Reform and the Restructuring of Central-Local Relations," in Goodman and Segal (fn. 56), 87–89; see also *New York Times*, November 23, 1993, p. 1.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

sive actions to preserve their reputation for discipline. I shall elaborate on these in turn.

Whereas Gorbachev's reformers identified "stagnation" as a key shortcoming of the CPSU and Komsomol, Chinese Communist Party (CCP) leaders were forced to rebuild unstable political institutions severely weakened by a decade of Cultural Revolution.[59] (The Chinese youth league needed to be reconstituted entirely and played a far more marginal role than its wealthy Soviet counterpart.) Central control over CCP local committees was already highly decentralized, and initiatives to deepen "intra-Party democracy" or devolve power to lower levels of the apparatus never advanced beyond the stage of rhetoric. Instead, "normalization" of Party life was stressed, which in practice meant avoiding further organizational upheaval within the Party.

As economic reform progressed, therefore, and CCP officials at local levels gained access to new sources of revenue retained by local and regional jurisdictions, they did not face the same uncertainties over Party tenure or funding confronted by their CPSU counterparts. Whereas new forms of economic organization in the Soviet Union became the sponges for assets withdrawn from the Party or Komsomol, analogous economic developments in China swelled local Party coffers without triggering an intra-Party bank run. Intra-Party discipline was only one centripetal factor, however; at least as important were the incentives established by the economic and fiscal reforms themselves.

Chinese economic reforms depended critically on empowering regional and rural officials as engines of economic growth. The hallmark of the reforms was the creation of hybrid organizational forms to control rural enterprises.[60] These hybrids represented a "virtual partnership" between enterprise management and local government.[61] Jean Oi has described this organizational innovation as "local state corporatism," arguing that it represented a "merger of state and economy" in which "fiscal reform has assigned local government property rights over increased income."[62]

The delegation of property rights to midlevel administration was not entirely an innovation of the Deng reforms; the Chinese system had long been less centralized than the Soviet system. David Granick has

[59] On CCP reforms, see White (fn. 55), 170–97.

[60] Nee (fn. 55), 2, defines hybrids as organizational forms that "use resources and/or governance structures from more than one existing organization."

[61] Ibid., 11.

[62] Oi, "Fiscal Reform and the Economic Foundations of Local State Corporatism in China," *World Politics* 45 (October 1992), 100.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

argued that such property rights originated in some cases as early as 1957 and were fairly stable from the early 1970s on; the Deng reforms, in this view, changed the scope of these rights.[63] This interpretation has been challenged by Susan Shirk, who argues that even under Deng devolution of power to local governments ran little risk of "loss of central control" because the center never lost the power to appoint local officials.[64] The analysis in this article suggests, first, that it is important to ask why the center has retained this power even as agents increasingly gained the resources to "defect,"[65] and second, that the critical distinction may be less the center-periphery allocation of property rights than the way in which those rights delineated public and private spheres.

Local officials profit from reform both by collection of higher levels of taxes and by direct profit sharing in quasi-public rural enterprises. The reforms have thus created "cadre-entrepreneurs" whose economic interests are tied to property rights that codify local government's role as shareholder and/or tax authority.[66] These cadre-entrepreneurs—frequently including local Party secretaries—have incentives similar to those of private businessmen, but they rely on their position in the state bureaucracy to preserve their "quasi-ownership rights."[67] Thus, the Chinese reforms served to reinforce the state's property rights rather than undermine them. Chinese local officials seeking to profit through the commercial deployment of state assets were not driven to move these assets out of the state sector, as in the Soviet case; rather, they faced powerful incentives to keep their state/Party position and accept whatever discipline was necessary to retain it.

The new incentive structure facing officials at the local levels in China is aptly expressed by the term "contracting" to describe the schemes put in place during the 1980s.[68] Beginning in 1981 enterprise managers were guided by "contracts" stipulating either tax or profit tar-

[63] David Granick, *Chinese State Enterprises: A Regional Property Rights Analysis* (Chicago: University of Chicago Press, 1990), 48. Zhao Suisheng also traces the roots of local powers into the pre-Deng era, describing a pattern of decentralization and recentralization from 1957 through the 1970s; Suisheng, "China's Central Local Relationship: A Historical Perspective," in Hao and Zhimin (fn. 55).

[64] Shirk (fn. 55), 150 fn. 2.

[65] Prior to the November 1993 CCP plenum, for instance, a significant number of provincial Party secretaries and governors were either rotated or retired, including the Party secretary of Jiangsu, China's richest province; see Yang (fn. 58), 86.

[66] Nee (fn. 55), 13.

[67] Shirk (fn. 55), 196. The term "quasi-ownership" is appropriate because the hybrid structure of the new rural enterprises assigned property rights to different organizations rather than to individuals. This position was advantageous either to a private businessman, who lacked the local official's control over supply networks, interregional trade, and tax rates, or to purely governmental actors, who collected fewer rents.

[68] See, for instance, the description by Christine P. Wong, "Fiscal Reform and Local Industrialization," *Modern China* 18 (April 1992), 216ff.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

gets on a multiyear basis.[69] Since 1987 regional governments were similarly guided by fiscal contracts negotiated with the center, stipulating regional contributions to (or subsidies from) the central budget. These reforms have not weakened the center at the expense of the provinces, as has sometimes been alleged; rather, careful studies of the Chinese fiscal system suggest that "the overall decline in budgetary revenues, rather than a change in the distribution of those revenues between center and local . . . is the more important trend of the reform era."[70]

Walder has characterized the effect of these reforms as producing a shift from "hierarchical authority" to "bilateral contracting," but the more remarkable feature of this transformation is that—unlike in the Soviet case—these new "contracts" have proved enforceable.[71] "State and Party officials" continue to exercise "all rights to control, income flows, and sale or liquidation" from both TVEs and state firms.[72] Regional governments continue to forward tax payments to Beijing.[73] The central government has even been able to recentralize some fiscal and financial functions, first during the 1988–89 retrenchment and more recently (though less effectively) during the 1993–94 "rationalizations" surrounding the Third Plenum of the Fourteenth Party Congress.[74] In other words, in China policies aimed at decentralization actually produced decentralization, and not a Soviet-style bank run.

In addition to creating incentives for preserving some hierarchical links, the Chinese reforms also left in place—indeed, even strength-

[69] This came to be known later as the Contract (or Enterprise) Responsibility System.

[70] Barry Naughton, "Implications of the State Monopoly over Industry and Its Relaxation," *Modern China* 18 (January 1992), 35. The point is reinforced by Christine P. W. Wong, "Central-Local Relations in an Era of Fiscal Decline: The Paradox of Fiscal Decentralization in Post-Mao China," *China Quarterly* 128 (December 1991).

[71] Andrew Walder, "Corporate Organization and Local Government Property Rights in China," in Vedat Milor, ed., *Changing Political Economies: Privatization in Post-Communist and Reforming States* (Boulder, Colo.: Lynne Rienner, 1994). In the formulation advanced in Section II above, however, hierarchical authority is simply presented as a form of bilateral contracting, i.e., a chain of agency contracts. In either Walder's formulation or mine, however, the critical question is whether these "contracts" can be enforced by either actor.

[72] Walder (fn. 71), 64.

[73] The center's share of tax revenues actually grew in the early 1980s and stabilized at about 30% (adjusted for borrowing) after the introduction of fiscal contracting in 1987. Though local governments tried various schemes to minimize their fiscal obligations to the center, they continued to "share up" revenues to Beijing. See Roy Bahl and Christine Wallich, "Intergovernmental Fiscal Relations in China," Policy Research Working Paper WPS 863 (Washington, D.C.: World Bank, February 1992); Wong (fn. 70), esp. 700–706; and Jia Hao and Wang Mingxia, "Market and State: Changing Central-Local Relations in China," in Hao and Zhimin (fn. 55), esp. 49–50.

[74] Dali L. Yang, "Policy Credibility and Macroeconomic Control in China" (Paper presented at the annual meeting of the American Political Science Association, Washington, D.C., 1993); and Yang (fn. 58). See also Yingyi Qian and Barry R. Weingast, "Beyond Decentralization: Preserving Federalism with Chinese Characteristics" (Manuscript, Stanford University, July 1994); and Jia Hao and Lin Zhimin, "Introduction," in Hao and Zhimin (fn. 55).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ened—the management information system previously based on central planning. The planning system itself was dismantled far more gradually than in the Soviet case, avoiding the information vacuum that crippled Soviet leaders.[75] The tax and profit contracting systems erected in its place gave officials greater incentives to monitor the economic activities of their subordinates. While the soft budget constraint continued to shield branch managers in the Soviet system, Chinese local officials quickly saw the fiscal incentives to maximize their revenue. Their incomes—both their bonuses and their budgets—were directly tied to the economic performance of enterprises under their jurisdiction.[76] In other words, local officials were rewarded for addressing precisely those problems of hidden action and hidden information that during the Soviet reform period had only been exacerbated.

This Chinese fiscal policy of "eating in separate kitchens" introduced a new challenge to the control exercised by the center, however.[77] Although local authorities directly retained a share of profits on rural enterprises, tax rates were still set at the center (unilaterally or through negotiation with the regions). Local authorities in economically active areas thus began manipulating the balance between rural enterprise budgets and profit remittances to minimize the revenues that had to be shared with the center. They have also begun to levy ad hoc fees and to raid extrabudgetary funds (that is, reserves) maintained by enterprises for the purpose of strategic investment. In response to this fiscal crunch, rural enterprises have been forced to submit to increasing levels of microlevel intervention by state actors. The result has been increasing manipulation of profit and budget figures by rural cadre-entrepreneurs, which will make it more difficult for officials in Beijing to monitor field-level activities and maintain their control.

Finally, the CCP's actions in Tiananmen Square during the summer of 1989 can be viewed as an explicit strategy to establish a reputation for punishing transgressions of discipline and deterring waves of opportunism. Reforms were thoroughly advanced by this time, however—so the leadership's reputation must already have been well established. As I discuss above, reputational strategies involve trading short-term costs for long-term deterrence. In this regard, the early agricultural successes of the Chinese reforms may have offered it deeper pockets to ab-

[75] In particular, Chinese authorities retained centralized control over heavy industry, which comprised a far smaller share of the Chinese economy than it did of the Soviet economy. Barry Naughton has called the Chinese approach "growing out of the Plan."

[76] See Oi (fn. 62), 114.

[77] This point is based largely on the analysis in Wong (fn. 70).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

sorb such short-term costs through the 1980s. More significantly, at the time of the June 1989 massacre, leaders in Beijing were already implementing an economic austerity program with only limited resistance from state and Party officials.

By contrast, institutions like the Komsomol and CPSU were already unpopular and weak by the time Gorbachev assumed the helm, and his abortive antialcohol campaign of 1985–88 was an unfortunate choice of policy on which to build a reputation for discipline. By the time local authorities began defying Moscow, the institutions at the center had little cushion with which to absorb short-term costs in the interests of seeking long-term equilibrium. By 1989 many Party and Komsomol leaders were already playing a short-term game themselves, and by 1991 not even army leaders could be counted on to remain under strict hierarchical control.

## V. Conclusions

As Yasheng Huang noted in a recent comparison of the choice of reform strategies in China and the Soviet Union, "administrative capacities matter."[78] While this is undoubtedly true, the analysis in this paper suggests that during periods of reform administrative capacities are not fixed. This article has attempted to show that institutions thought to be "guiding" a reform can be profoundly weakened by the very reforms they unleash. In an environment of rapid change, opportunistic agents at lower levels of the bureaucratic hierarchy may perceive a chance to profit from chaos and seize the assets they have been managing as their superiors lose the authority to exercise discipline. Thus, institutional stability must be viewed as endogenous to models of reform.

The model also suggests that erosion of hierarchical authority is not inevitable. Certain institutional characteristics may help insulate an organization from the centrifugal forces described here, and elements of the institutional reforms themselves or the actions of political leaders can affect the calculations of lower-level bureaucrats. In the Chinese case, leaders have thus far managed to grant greater autonomy to local officials without completely eroding the basic authority links within structures like the CCP, TVE, or state-fiscal systems.

In particular, the comparison of the Soviet and Chinese cases illustrates several key insights of the agency model that help explain differ-

[78] Huang, "Information, Bureaucracy, and Economic Reforms in China and the Soviet Union," *World Politics* 47 (October 1994), 134.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ences in the consequences of the respective reforms.[79] As Soviet officials devolved control over budgets and revenue sources, they exacerbated information asymmetries between principals and agents and permitted opportunistic agents to use accumulated safety margins to seize assets under their control. These acts of defiance quickly escalated into a bank run, as officials in Moscow acted, not to discipline agents, but to protect their own assets. In China, by contrast, more extensive devolution of fiscal and economic power created new incentives for monitoring agents at lower levels of the bureaucracy, and top officials signaled that there were limits to their tolerance of overt defiance. The Chinese system was also less centralized to begin with, so ratchet effects were less prevalent and accumulated safety margins less pervasive. Though some regional officials have negotiated aggressively with Beijing to gain economic advantages, the basic structure of the Chinese economic, state-fiscal, and political systems has remained comparatively stable.

The model suggests that the lessons drawn from the Chinese case must be carefully considered. The hidden hand behind the Chinese market wielded a bloody bayonet, but it also presided over a broad reallocation of property rights. As a consequence, bureaucrats hoping to profit from economic reforms faced strong incentives to remain in their state and Party positions, rather than attempt to "privatize" assets under their control. Some China scholars have called the reforms "botched" because they replaced state intervention at the center with state intervention in the localities,[80] but this same decentralization of quasi-ownership rights may have provided crucial organizational glue for holding the state and Party together.

This analysis suggests that Chinese institutions are likely to be subjected to growing centrifugal forces, particularly after the death of Deng. In recent years a variety of regional challenges to Beijing's rule have led to dire warnings about the "disintegration of the national economy into thousands of fief-like county and provincial economies."[81] The private business sector has begun to expand rapidly and could offer today's cadre-entrepreneurs the potential to trade quasi-ownership rights for private ownership.[82] Though hybrid organizations

[79] These findings are summarized at the beginning of Section IV.

[80] Wong (fn. 70), 711–13. Chinese reforms have also been criticized for unleashing massive corruption, but this was also characteristic of the Soviet reforms.

[81] Nee (fn. 55), 6.

[82] The anticorruption drives launched by Chinese leaders in the last year or two may accelerate this process if they convince local officials that their property rights may be made more secure by leaving their official posts, even at the cost of future rent-seeking opportunities.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

continue to enjoy several important advantages over private enterprises in the partially marketized Chinese system, those advantages may begin to diminish as the private sector grows.[83] At that point, Chinese institutions may face a risk of an organizational bank run similar to that of the late Soviet period.

One important check on the privatization of Chinese regional economies, however, will be those regions that remain opposed to reform. In the Soviet case assets of organizations like the Party and Komsomol were widely distributed and almost universally redeployable in newly private ventures. In China regional development has been highly unequal, and successful regions are growing more skillful at shielding revenues from Beijing.[84] Thus, a bank run could also be triggered by "conservative" regions attempting a more comprehensive redistribution of assets from richer regions.

The Chinese experience does have some potentially important consequences for actors in the post-Soviet environment. The hidden action and hidden information problems that plagued Soviet organizations continue to afflict new post-Soviet institutions. Information flows in the post-Soviet system remain highly distorted, and budget constraints remain malleable.[85] Under these conditions, the Chinese experience with hybrid organizational forms combining state and private ownership may prove important. By allowing regional and municipal actors to hold a stake in emerging regional "holding companies," Russian officials may at least reduce the incentives of these actors to undermine the authority and property rights of central authorities.

In essence, such an approach may represent the institutionalization of rent seeking as the price of institutional stability. Unfortunately for reformers, however, in Russia (and other transitional systems where property rights are ambiguous or uncertain) organizational structures are likely to remain unstable unless and until agents perceive clear incentives to accept hierarchical authority once again.

[83] Nee (fn. 55), 8–22.

[84] Several techniques are described in Wang Shaogang, "Central-Local Fiscal Politics in China," in Hao and Zhimin (fn. 55).

[85] In addition, Russian leaders have since 1992 been unable to build a reputation for retaliating against regional defiance. The debacle in Chechnya may only make matters worse by demonstrating the prohibitive cost of such retaliation.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# STABILITY AND THE DISTRIBUTION OF POWER

By ROBERT POWELL*

THE relation between the distribution of power and the probability of war has been at the center of a long and important debate in international relations theory. Is an even distribution of power more or less stable than a preponderance of power? The balance-of-power school generally argues that an even distribution of power is more stable, whereas the preponderance-of-power school generally argues the opposite, that a preponderance of power is more stable.[1]

Empirical efforts to resolve this debate have yielded equivocal results. Siverson and Tennefoss, for example, find an even distribution of power to be more stable, whereas Kim and Moul find a preponderance of power to be more stable. Singer, Bremer, and Stuckey find an even distribution to be more stable than a preponderance of power during the nineteenth century and the opposite during the twentieth century. Maoz and Bueno de Mesquita and Lalman, by contrast, find no significant relation between the probability of war and the distribution of power. Finally, Mansfield finds evidence of a nonlinear, quadratic relation in which the probability of war is smallest when there is an even distribution and a preponderance of power.[2]

* I am grateful to Bruce Bueno de Mesquita, James Fearon, Joanne Gowa, Robert Keohane, James Morrow, Paul Papayoanou, Leo Simon, R. Harrison Wagner, and Barry Weingast for their comments and criticisms. This work was assisted by a grant from the National Science Foundation (SES 9121959) and a National Fellowship at the Hoover Institution at Stanford University.

[1] Arguing that a balance is more stable are Innis Claude, *Power and International Relations* (New York: Random House, 1962); Hans Morgenthau, *Politics among Nations*, 4th ed. (New York: Alfred Knopf, 1967); John Mearsheimer, "Back to the Future," *International Security* 15 (Summer 1990); Quincy Wright, *A Study of War* (Chicago: University of Chicago Press, 1965); and Arnold Wolfers, *Discord and Collaboration* (Baltimore: Johns Hopkins University Press, 1962). Arguing that a preponderance is more stable are Geoffrey Blainey, *The Causes of War* (New York: Free Press, 1973); A. F. K. Organski, *World Politics* (New York: Alfred A. Knopf, 1968); and A. F. K. Organski and Jacek Kugler *The War Ledger* (Chicago: University of Chicago Press, 1980). For a review of this debate, see Jack Levy, "The Causes of War: A Review of Theories and Evidence," in Philip Tetlock et al., eds., *Behavior, Society, and Nuclear War*, vol. 1 (New York: Oxford University Press, 1989); for a discussion of some of the important conceptual issues, see R. Harrison Wagner, "Peace, War, and the Balance of Power," *American Political Science Review* 88 (September 1994).

[2] Randolph Siverson and Michael Tennefoss, "Power, Alliance, and the Escalation of International Conflict, 1815–1965," *American Political Science Review* 78 (December 1984); Woosang Kim, "Alliance Transitions and Great Power War," *American Journal of Political Science* 35 (November 1991); idem,



LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Claims about the relation between the distribution of power and the likelihood of war have generally lacked any formal foundations. Some recent work has attempted to fill this gap, however. Bueno de Mesquita and Lalman and Fearon analyze models of international bargaining. The former find, first, that the probability of war is smallest when the distribution of power is uneven and, second, that "dissatisfaction with the status quo is unrelated to the likelihood of war."[3] Fearon, by constrast, finds that the probability of war is independent of the distribution of power; that is, a change in the distribution of power has no effect on the likelihood of war.[4]

This essay examines the relation between the probability of war and the distribution of power in the context of a game-theoretic model in which two states are bargaining about revising the international status quo. In the model the states make proposals for changing the status quo. The bargaining continues until the states reach a mutually acceptable settlement or until one of them becomes sufficiently pessimistic about the prospects of reaching an agreement that it uses force to try to impose a new international order. The states' equilibrium strategies specify the demands the states will make of each other and the circumstances in which they will resort to force. The equilibrium strategies thus make it possible to calculate the probability that bargaining will break down in war as a function of the distribution of power between the two states. The shape of this function can then be compared to the relation claimed to exist by the balance-of-power and preponderance-of-power schools.

The probability of war in the model turns out to be a function of the disparity between the status quo distribution of benefits and the distribution expected to result from the use of force. The outcome expected from using force is, in turn, directly related to the distribution of power.

---

"Power Transitions and Great Power War from Westphalia to Waterloo," *World Politics* 45 (October 1992); William Moul, "Balances of Power and the Escalation to War of Serious International Disputes among the European Great Powers, 1815–1939," *American Journal of Political Science* 32 (February 1988); J. David Singer, Stuart Bremer, and John Stuckey, "Capability Distribution, Uncertainty, and Major Power War, 1820–1965," in Bruce Russett, ed., *Peace, War, and Numbers* (Beverly Hills, Calif.: Sage, 1972); Zeev Maoz, "Resolve, Capabilities, and the Outcomes of Interstate Disputes, 1815–1976," *Journal of Conflict Resolution* 27 (June 1983); Bruce Bueno de Mesquita and David Lalman, "Empirical Support for Systemic and Dyadic Explanations of International Conflict," *World Politics* 41 (October 1988); idem, *Reason and War* (New Haven: Yale University Press, 1992); Edward Mansfield, "The Concentration of Capabilities and the Onset of War," *Journal of Conflict Resolution* 36 (March 1992); idem, *Power, Trade, and War* (Princeton: Princeton University Press, 1994).

[3] Bueno de Mesquita and Lalman (fn. 2, 1992), 204–5, 190.

[4] James Fearon, "War, Relative Power, and Private Information" (Paper presented at the annual meeting of the International Studies Association, Atlanta, March 31–April 4, 1992), 20.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Thus, the probability of war is a function of the disparity between the status quo and the distribution of power. When this disparity is small, the division of benefits expected from the use of force is approximately the same as the existing status quo distribution. The gains to using force are therefore too small to outweigh the costs of fighting. Neither state is willing to use force to change the status quo, and the probability of war is zero. When the disparity between the status quo division of benefits and the distribution of power is large, then at least one state is willing to use force to overturn the status quo. Moreover, as the disparity grows, the probability of war generally increases.

These results seem quite intuitive: as the disparity between the distribution of power and the distribution of benefits grows, the probability of war generally increases. Indeed, this formal result echoes Gilpin's explanation of hegemonic wars.[5] Such wars arise, he argues, because of a disparity between the distribution of power and the international status quo distribution of benefits imposed by the hegemon following the previous hegemonic war.[6] Although intuitive, these results contradict the expectations of both the balance-of-power and preponderance-of-power schools. The former expects the probability of war to be smallest when power is evenly distributed, but the probability of war is smallest in the present model when the distribution of power mirrors the status quo distribution of territory. These claims will coincide only in the special case in which the status quo distribution is even. The preponderance-of-power school expects the probability of war to be smallest when the distribution of power is highly skewed and to increase as the distribution of power becomes more even. But the probability of war is largest in the model developed below when the distribution of power is highly skewed.

The formal results derived here also differ from those obtained by Fearon and Bueno de Mesquita and Lalman. Unlike Fearon, the probability of war in the present formulation does vary with changes in the distribution of power.[7] Unlike Bueno de Mesquita and Lalman, who find that "dissatisfaction with the status quo is unrelated to the likelihood of war" and that the probability of war declines as the distribu-

[5] Robert Gilpin, *War and Change in World Politics* (Cambridge: Cambridge University Press, 1981).

[6] Although the potential use of force is not the source of the coercive pressure, some suggest that international regimes are more likely to break down when the underlying distribution of power differs from the distribution of benefits the regime confers. See Robert Keohane and Joseph Nye, *Power and Interdependence* (Boston: Little Brown, 1977), 139; and Stephen Krasner, "Regimes and the Limits of Realism," in Krasner, ed., *International Regimes* (Ithaca, N.Y.: Cornell University Press, 1983), 357–58,

[7] Fearon (fn. 4).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tion of power becomes more skewed, the probability of war is directly related to the level of dissatisfaction with the status quo and generally increases as the distribution of power becomes more skewed.[8]

The remainder of this essay is organized as follows. The next section motivates and defines the model and discusses some qualifications and limitations. The subsequent section describes the game's equilibrium. The final section uses this equilibrium to specify the probability of war as a function of the distribution of power and compares these results with the expectations of the balance-of-power and preponderance-of-power schools and with other formal work. That section also offers a possible explanation for the equivocal empirical results of efforts to measure the relation between stability and the distribution of power.

## The Model

To motivate the model, suppose two states are bargaining about revising the international status quo. More concretely, imagine that two states are negotiating about changing the territorial status quo. Each state proposes a division of the territory that the other state can accept or reject. The bargaining continues with offer followed by counteroffer until the states agree on a proposed division or until one of the states becomes sufficiently pessimistic about the prospects of reaching a mutually acceptable settlement that it resorts to force to try to impose a new territorial settlement.[9]

How do changes in the distribution of power between these two states affect the bargaining and, more specifically, the probability that the bargaining will break down in war? Are the negotiations more likely to break down if one state has a preponderance of power or if there is an even distribution of power? It might seem at first that the preponderance-of-power school is clearly correct and that the bargaining is less likely to break down if one of the states has a preponderance of power. That is, suppose a state, say $S_1$, has just proposed a particular division to the other state $S_2$. $S_2$ would be tempted to use force to impose a settlement rather than accept $S_1$'s offer only if the expected payoff to using force were at least as large as the payoff to agreeing to the proposal. But the weaker $S_2$, the lower its expected payoff to fighting. In-

[8] Bueno de Mesquita and Lalman (fn. 2, 1992), 190, 204–5.

[9] In a more general model the two states might be bargaining about altering the international status quo where the set of feasible outcomes is an n-dimensional policy space. Each point in this space represents a different international order and a different distribution of benefits for the two states. The formal analysis developed below applies equally well to this more general formulation.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

deed, if $S_2$ is sufficiently weak, its payoff to using force will be less than its payoff to agreeing to $S_1$'s offer. In this case, $S_2$ will acquiesce to $S_1$'s demand and will not be tempted to use force. Nor will $S_1$ be tempted to use force, since $S_2$ is willing to agree to $S_1$'s demand. This reasoning, which suggests that a preponderance of power will be more stable, is essentially the reasoning Organski advances: "A preponderance of power . . . increases the chances of peace, for the greatly stronger side need not fight at all to get what it wants, while the weaker side would be plainly foolish to attempt battle for what it wants."[10]

There is, however, a countervailing factor at work. The preceding argument was based on the assumption that $S_1$'s proposal was fixed. But as $S_1$ becomes stronger and $S_2$ becomes weaker, $S_1$ knows that $S_2$ is more likely to accept any given proposal. Thus, $S_1$ will demand more of $S_2$ as $S_2$ becomes weaker. $S_2$, in turn, may be more likely to resist these larger demands, and war may become more likely when there is a preponderance of power. If so, then a preponderance of power would be less stable. By contrast, an even distribution of power would restrain all states' demands and thereby enhance stability. This restraining effect of an even distribution of power underlies the balance-of-power school's analysis of the relation between stability and the distribution of power. As Wolfers argues, "Thus, from the point of view of preserving the peace . . . it may be a valid proposition that a balance of power placing restraint on every nation is more advantageous in the long run than the hegemony even of those deemed peace-loving at the time."[11]

In sum, a shift in the balance of power against $S_2$ has two competing effects. First, $S_2$ is more likely to accept any specific demand. But, second, more will be demanded of it than would have been had it been more powerful. The first effect tends to make war less likely, while the second tends to make war more likely. The net result of these two opposing effects on the probability of war is unclear: whereas the preponderance-of-power school emphasizes the first effect, the balance-of-power school underscores the second effect. The game-theoretic model of bargaining developed here makes it possible to weigh the interaction of these two competing effects more formally.

Rubinstein's seminal analysis of an alternating-offer, infinite-horizon bargaining game provides a point of departure for the present analysis.[12] In Rubinstein's model two actors are trying to divide a pie. One actor begins the game by proposing a division of the pie to the other,

[10] Organski (fn. 1), 294.
[11] Wolfers (fn. 1), 120. See also Claude (fn. 1), 62.
[12] Ariel Rubinstein, "Perfect Equilibrium in a Bargaining Model," *Econometrica* 50 (January 1982).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

who can either accept or reject the offer. Acceptance ends the game and the pie is divided as agreed. If the second actor rejects the initial proposal, it makes a counteroffer that the first actor can either accept or reject. Acceptance again ends the game. If the first actor rejects the proposal, it makes a new offer. The actors alternate making offers until they agree on a division.[13]

The present model adds the option of using force to Rubinstein's basic structure. As illustrated in Figure 1, $S_1$ begins the game by proposing a division of the status quo. More formally, $S_1$ demands some fraction $x$ of the disputed territory where $x$ lies between zero and one. If, for example, $S_1$ sets $x = 1$, then $S_1$ is demanding all of the territory for itself; if $S_1$ sets $x = 1/2$, it is demanding half of the territory; and if $S_1$ sets $x = 0$, it is offering $S_2$ all of the territory. (The arc between "0" and "1" in Figure 1 indicates that a state can demand any fraction between 0 and 1.) $S_2$ can accept this offer by saying yes, which is denoted by *Y*; reject it by saying no, *N*, and subsequently make a counteroffer; or force a settlement by attacking $S_1$ with *A*. The game ends if $S_2$ accepts or attacks. If $S_2$ rejects, it then proposes a new territorial division. $S_1$ can now accept, reject, or attack. As before, accepting or attacking ends the game. If $S_1$ rejects, it again suggests another division. The bargaining continues, possibly forever, with offers alternating back and forth until one of the states accepts a proposal or attacks.

To specify the states' payoffs, let $(q, 1 - q)$ denote the status quo division where $q$ and $1 - q$ are $S_1$'s and $S_2$'s respective shares. Now suppose that the states agree to divide the territory according to $(x, 1 - x)$ where $S_1$ and $S_2$ receive $x$ and $1 - x$, respectively. Assume further that this agreement is reached at time $t$, that is, after $t + 1$ offers. (For notational convenience, the first offer is made at time $t = 0$.) If agreement is reached at time $t$, then $S_1$ had $q$ and $S_2$ had $1 - q$ from the beginning of the game until time $t - 1$. The payoff that $S_1$ derives from having a flow of $q$ for the first $t$ periods will be taken to be $U_1(q) + \delta U_1(q) + \delta^2 U_1(q) + \cdots + \delta^{t-1} U_1(q) = (1 - \delta^t) U_1(q)/(1 - \delta)$ where $\delta$ is the states' common discount factor and $U_1$ is $S_1$'s utility function for benefits. $S_1$ will also be assumed to prefer larger allocations to smaller allocations but with a nonincreasing marginal value.[14] Once agreement is reached at time $t$, $S_1$'s allocation from time $t$ forward is $x$. The present value of having $x$ from time $t$ forward is $\delta^t U_1(x) + \delta^{t+1} U_1(x) + \delta^{t+2} U_1(x) + \cdots = \delta^t U_1(x)/(1 - \delta)$. Thus, $S_1$'s payoff to agreeing to $(x, 1 - x)$ at time $t$ is $(1 - \delta^t) U_1(q)/(1 - \delta) + \delta^t U_1(x)/(1 - \delta)$. Similarly, $S_2$'s payoff to agree-

[13] Rubinstein (fn. 12) showed that this game has a unique subgame-perfect equilibrium.

[14] More formally, $U_1$ is assumed to be twice differentiable with $U_1' > 0$ and $U_1'' \leq 0$. $S_1$ is risk neutral if $U_1'' = 0$ and risk averse if $U_1'' < 0$.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

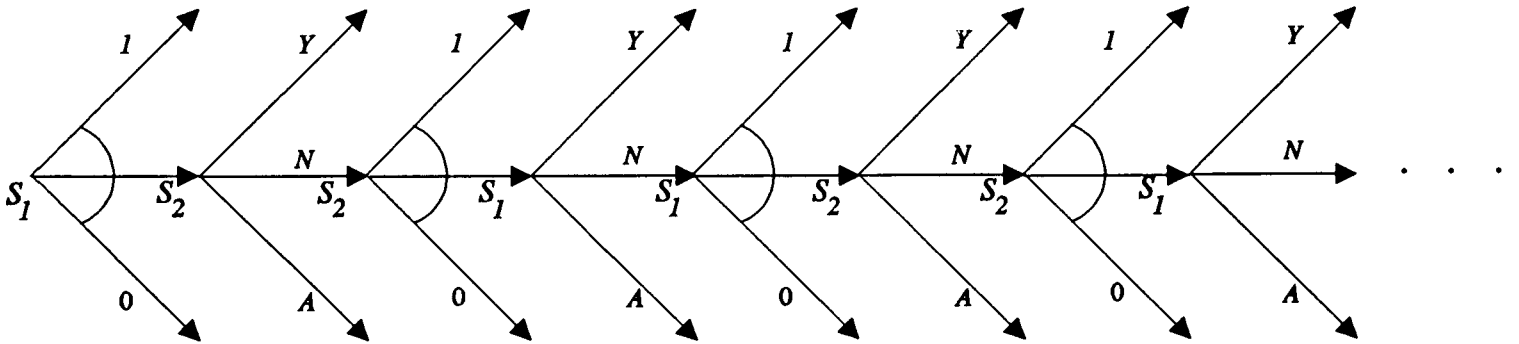



FIGURE 1
AN INFINITE-HORIZON, ALTERNATING-OFFER GAME WITH THE OPTION OF USING FORCE

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ing to $(x, 1-x)$ at time $t$ is $(1-\delta^t)U_2(1-q)/(1-\delta) + \delta^t U_2(1-x)/(1-\delta)$ where $U_2$ is $S_2$'s utility.

To define the states' payoffs if they fail to reach an agreement and one of them uses force, suppose that they fight at time $t$. As before, $S_1$ derives $(1-\delta^t)U_1(q)/(1-\delta)$ from having $q$ during the first $t$ periods. To simplify the specification of $S_1$'s payoff following an attack, war will be assumed to end in one of only two ways. Either $S_1$ will be completely victorious, or $S_2$ will be. (The limitations of this simplification are discussed below.) If $S_1$ prevails, it takes all of the territory at a cost of fighting $c_1$. The payoff to having all of the territory less the cost of fighting from time $t$ forward is $\delta^t(U_1(1)-c_1) + \delta^{t+1}(U_1(1)-c_1) + \delta^{t+2}(U_1(1)-c_1) + \ldots = \delta^t(U_1(1)-c_1)/(1-\delta)$. If $S_1$ loses, $S_2$ captures all of the territory which leaves $S_1$ with nothing but the cost of fighting. The payoff to this outcome is $\delta^t(U_1(0)-c_1) + \delta^{t+1}(U_1(0)-c_1) + \delta^{t+2}(U_1(0)-c_1) + \ldots = \delta^t(U_1(0)-c_1)/(1-\delta)$.

Going to war is an uncertain venture. Let $p$ reflect the balance of power or the distribution of capabilities between $S_1$ and $S_2$. That is, $p$, which is assumed to be common knowledge, is the probability that $S_1$ will prevail if force is used.[15] Then $S_1$'s expected payoff to a bargaining process that ends in war at time $t$ is the value of living with the status quo until time $t-1$ plus the payoff to prevailing at time $t$ times the probability of prevailing, $p$, plus the payoff to losing at time $t$ times the probability of losing, $1-p$:

$$\frac{(1-\delta^t)U_1(q)}{1-\delta} + p\,\frac{\delta^t(U_1(1)-c_1)}{1-\delta} + (1-p)\,\frac{\delta^t(U_1(0)-c_1)}{1-\delta}\quad .$$

This payoff can be simplified by normalizing the utility function by setting the payoff to having all of the territory equal to one and the payoff to having no territory equal to zero (that is, $U_1(1) = 1$ and $U_1(0) = 0$). Letting $W_1(t)$ and $W_2(t)$ denote $S_1$'s and $S_2$'s normalized payoffs to a bargaining process that ends in war at time $t$ leaves:

$$W_1(t) = \left(\frac{1-\delta^t}{1-\delta}\right) U_1(q) + \frac{\delta^t}{1-\delta}\,(p-c_1)$$

$$W_2(t) = \left(\frac{1-\delta^t}{1-\delta}\right) U_2(1-q) + \frac{\delta^t}{1-\delta}\,(1-p-c_2)\,.$$

[15] There are no offensive or defensive advantages in the present formulation, so it makes no difference whether $S_1$ or $S_2$ attacks.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

The model developed so far has complete information. Each state knows the other state's payoffs. As discussed more fully below, as long as information is complete, bargaining never breaks down, regardless of the distribution of power. In this model incomplete information is a prerequisite to war. In the next section each state is assumed to be uncertain of the other's willingness to use force.

Before turning to incomplete information and an analysis of the game's equilibrium, however, it will be useful to consider some of the limitations and qualifications of the model. The most significant limitation is that there are only two states. One argument about the relation between stability and the distribution of power emphasizes the importance of the number of coalitions that could form to block any state's bid for hegemony. The larger the number of states and the more even the distribution of power, the larger the number of potential blocking coalitions and the less likely is war.[16] As a formal analysis of this argument clearly requires a model in which there are more than two actors, it is beyond the scope of the present analysis.[17]

It is important to emphasize, however, that although some arguments about the relation between the distribution of power and the probability of war presuppose the existence of more than two states, other arguments do not. Wright, for example, explicitly considers the situation in which there are only two states. In this case, balance-of-power theory expects that "there would be great instability unless [the two states] were very nearly equal in power or their frontiers were widely separated or difficult to pass."[18] Similarly, Mearsheimer considers the case of two great powers and claims that a balance of power is more stable: "Power can be more or less equally distributed among the major powers of both bipolar and multipolar systems. *Both* are more peaceful when equality is greatest among the poles."[19] In sum, the conflicting claims of the balance-of-power and preponderance-of-power schools apply to systems in which there are only two states, as well as to systems with more than two states. The present analysis focuses on the former case.

A second significant limitation of the model is that the distribution of power is fixed. But the key to several arguments about the relation

[16] See Levy (fn. 1), 231–32; Mansfield (fn. 2, 1994), 17–18; and Wright (fn. 1), 755.

[17] For efforts to examine the relation between stability and the distribution of power in a setting in which there are more than two states, see Emerson Niou and Peter Ordeshook, "Stability in Anarchic Internatonal Systems," *American Journal of Political Science* 84 (December 1990); Wagner (fn. 1); and idem, "The Theory of Games and the Balance of Power," *World Politics* 38 (July 1986).

[18] Wright (fn. 1), 755.

[19] Mearsheimer (fn. 1), 18; emphasis added.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

between the likelihood of war and the distribution of power is that this distribution shifts over time, perhaps because of uneven economic growth.[20] This raises an important problem, which is the effects of changes in the distribution of power over time on the probability of war. Unfortunately, it is beyond the scope of the present model and must await future work.[21]

Another seeming limitation is that war can result in only two possible outcomes: a state either wins all of the territory or loses all of it. This limitation is more apparent than real, however. The assumption that war can end in only two ways simplifies the notation and discussion, but it is not central to the analysis of the model. One might assume instead that war could result in any territorial division. Changes in the distribution of power would still be reflected in changes in the probability distribution over the now larger set of possible outcomes.

Furthermore, both states are assumed to agree on the distribution of power (that is, both states know $p$). This assumption not only simplifies the analysis but has some substantive import for international relations theory as well. Blainey and others argue that war results from uncertainty about the distribution of power.[22] While this uncertainty may be an important cause of war, it is not a necessary condition as Blainey suggests. The model serves as a counterexample to this claim: states agree on the distribution of power and yet there is war.[23]

Finally, the terms of the agreement do not affect the distribution of power. So, for example, an agreement that transfers a large amount of territory to one state does not make that state more powerful. Wagner argues that this may be an important cause of war, and extending the model to allow for this possibility would be relatively straightforward.[24]

## The Equilibrium

This section characterizes the game's equilibrium. To summarize the results, a state will be called dissatisfied if it prefers fighting to the status quo and satisfied if it prefers the status quo to fighting. If both states

[20] See, for example, Charles Doran and Wes Parsons, "War and the Cycle of Relative Power," *American Political Science Review* 74 (December 1980); Gilpin (fn. 5); Organski (fn. 1); and Organski and Kugler (fn. 1).

[21] For efforts in this direction, see Fearon (fn. 4); Woosang Kim and James Morrow, "When Do Power Transitions Lead to War?" *American Journal of Political Science* 36 (November 1992); and Powell, "Appeasement as a Game of Timing" (Manuscript, Department of Political Science, University of California, Berkeley, July 1995).

[22] Blainey (fn. 1).

[23] Fearon (fn. 4) first makes and develops this point.

[24] Wagner (fn. 1).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

are satisfied, then the status quo remains unchanged and the probability of war is zero, as neither state can credibly threaten to use force to overturn the status quo. If one of the states is dissatisfied, then the satisfied state makes its optimal offer to the dissatisfied state given the satisfied state's beliefs about the willingness of the dissatisfied state to use force. Although the dissatisfied state can always reject this offer and make a counteroffer, it never does so in equilibrium. Rather, the dissatisfied state either accepts this offer or attacks.[25] The next section uses these equilibrium strategies to calculate the probability of war as a function of the distribution of power. (Readers less interested in the derivation of these results may omit the rest of this section.)

Three preliminaries are needed before the equilibrium strategies can be specified. First, a dissatisfied state must be defined more precisely. Second, the equilibrium of the complete-information game must be described. Finally, incomplete information needs to be introduced.

A state is dissatisfied if it prefers fighting to living with the status quo. In symbols, $S_1$'s payoff to fighting now (that is, at $t = 0$) is $W_1(0) = (p - c_1)/(1 - \delta)$. $S_1$'s payoff to living with the status quo is $U_1(q)/(1 - \delta)$. Thus, $S_1$ is dissatisfied if $p - c_1 > U_1(q)$. Similarly, $S_2$ is dissatisfied if $1 - p - c_2 > U_2(1 - q)$. At most only one state can be dissatisfied.[26]

The complete-information game has a very simple equilibrium.[27] If both states are satisfied, then neither state can credibly threaten to use force to change the status quo. The status quo remains unaltered. If one of the states is dissatisfied, then the satisfied state offers just enough in equilibrium to the dissatisfied state to ensure that it will never find fighting worthwhile. In effect, the satisfied state appeases the dissatisfied state by offering it just enough to leave it indifferent between accepting the offer and fighting. In symbols, suppose that $S_1$ is the dissatisfied state. Then the satisfied state, $S_2$, will offer just enough, say $x$, so that the dissatisfied state's payoff to accepting $x$, $U_1(x)/(1 - \delta)$, is equal to the payoff to fighting, $(p - c_1)/(1 - \delta)$. Thus, $x$ satisfies $U_1(x) = p - c_1$. To see that this is $S_2$'s optimal offer, note that $S_2$ would never

[25] As will be seen, at most only one state can be dissatisfied.

[26] This follows from the assumptions that the states are risk neutral or risk averse, that they agree on the distribution of power, and that fighting is costly. Because the states are risk neutral or risk averse, the utility functions are concave, which implies $U_1(q) \geq q$ and $U_2(1 - q) \geq 1 - q$. If both states are dissatisfied, then $p - c_1 > U_1(q) \geq q$ and $1 - p - c_2 > U_2(1 - q) \geq 1 - q$. Adding these inequalities gives $1 - c_1 - c_2 > 1$ or $0 > c_1 + c_2$. But fighting is costly, so $c_1 \geq 0$ and $c_2 \geq 0$. Thus, $c_1 + c_2$ cannot be less than zero, and this contradiction implies that at least one state must be satisfied.

[27] The complete-information game is a straightforward modification of Rubinstein's (fn. 12) model with an outside option. For an analysis of the unique subgame-perfect equilibrium of this game, see Martin Osborne and Ariel Rubinstein, *Bargaining and Markets* (New York: Academic Press, 1990), 54–58.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

offer more than the minimum needed to appease $S_1$ and to ensure that it will not attack. Nor would $S_2$ offer less than this amount. $S_1$ would reject a smaller offer and fight, which would leave $S_2$ with a payoff of $(1 - p - c_2)/(1 - \delta)$. $S_2$, however, prefers the payoff of offering $x$ to $S_1$, which is $U_2(1 - x)/(1 - \delta)$.[28]

With complete information, bargaining never results in war regardless of the distribution of power. The satisfied state always offers the dissatisfied state just enough to appease it. By contrast, bargaining can end in war if there is incomplete information, because the satisfied state is uncertain of what is needed to appease the dissatisfied state. The more the satisfied state offers, the less likely the dissatisfied state will be to attack; but the more the satisfied state offers, the lower its payoff will be should the offer be accepted. The satisfied state must therefore balance these two effects when deciding how much to offer. Often the satisfied state will choose to accept some risk of war. With incomplete information, the relation between stability and the distribution of power is a live issue.

To introduce incomplete information formally, each state will be assumed to be uncertain of the other state's cost of fighting. In particular, $S_1$ is unsure of $S_2$'s cost of fighting $c_2$ but believes that this cost is at least $\underline{c}_2$ and not more than $\bar{c}_2$. The value $\underline{c}_2$, which is assumed to be nonnegative, is the lowest cost of fighting that $S_1$ believes $S_2$ might have. That is, if $S_2$'s cost is $\underline{c}_2$, $S_1$ is facing the toughest type of $S_2$. If $S_2$'s cost is $\bar{c}_2$, $S_1$ is facing the weakest possible type of $S_2$, that is, the type of $S_2$ for which fighting is most costly. Similarly, $S_2$ is unsure of $S_1$'s cost of fighting but believes that it is at least $\underline{c}_1$ and no more that $\bar{c}_1$. These beliefs are represented formally as probability distributions $F_1(c_1)$ and $F_2(c_2)$.[29]

Although $c_1$ and $c_2$ have been described as the states' costs of fighting, these variables also have a more general interpretation. The lower $c_1$, the higher $S_1$'s payoff to fighting. Accordingly, $c_1$ can be interpreted more generally as a measure of $S_1$'s willingness to use force or of $S_1$'s resolve. That is, the lower $c_1$, the more willing $S_1$ is to use force and the greater its resolve. Thus, the game may be seen more broadly as a model of bargaining between two states that are unsure of each other's willingness to use force.

The introduction of incomplete information necessitates a more refined definition of what it means to be dissatisfied. From $S_2$'s perspec-

[28] If $S_2$ preferred fighting to offering $x$, then $1 - p - c_2 > U_2(1 - x)$ where $p - c_1 = U_1(x)$. Adding these relations and recalling that $U_1$ and $U_2$ are concave leave the contradiction $0 > c_1 + c_2$.

[29] These cumulative distributions functions are assumed to have continuous densities that are positive over the intervals $(\underline{c}_1, \bar{c}_1)$ and $(\underline{c}_2, \bar{c}_2)$. These distributions are also common knowledge.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tive, $S_1$ can be any one of a continuum of types with costs ranging from $\underline{c}_1$ to $\bar{c}_1$. That is, $S_2$ is unsure of $S_1$'s type where $S_1$'s type is its cost of fighting. Similarly, $S_1$ is uncertain of $S_2$'s type where $S_2$'s type is its cost of fighting. Accordingly, a player type is dissatisfied if it prefers fighting to the status quo. So, type $c'_1$ of $S_1$ is dissatisfied if $p - c'_1 > U_1(q)$, and type $c'_2$ of $S_2$ is dissatisfied if $1 - p - c'_2 > U_2(1 - q)$. A player is potentially dissatisfied if there is some chance that it prefers fighting to the status quo. That is, a player is potentially dissatisfied if its toughest type is dissatisfied. Accordingly, $S_1$ is potentially dissatisfied if $p - \underline{c}_1 > U_1(q)$, and $S_2$ is potentially dissatisfied if $1 - p - \underline{c}_2 > U_2(1 - q)$. Paralleling the complete-information case, at most only one state can be potentially dissatisfied.

The incomplete-information game has a unique perfect Bayesian equilibrium outcome.[30] If both states are satisfied, then the outcome is trivial. Although each state is uncertain of the other's exact cost of fighting, each is sure the other's cost is so high that the other state will not fight to overturn the status quo. Thus, neither state can credibly threaten to use force to change the status quo. In equilibrium, the status quo goes unchanged, and the probability of war is zero.

The derivation of the equilibrium in the case in which one of the states is potentially dissatisfied is long and very detailed and is presented in full detail elsewhere.[31] The present discussion focuses on the central ideas underlying the proof. There are three major steps in the derivation. Assume without loss of generality that $S_1$ is the potentially dissatisfied state. Then the first step is to show that in equilibrium no dissatisfied type of $S_1$ will ever reject an offer from $S_2$ in order to make a counteroffer. A dissatisfied type will either accept the offer on the table or fight, depending on which alternative gives the higher payoff. Second, the fact that no dissatisfied type will ever make a counteroffer implies that all satisfied types will accept any offer larger than the status quo. The first two steps thus characterize the dissatisfied state's response to an offer from the satisfied state: If the satisfied state $S_2$ offers an $x$ that is larger than the dissatisfied state's status quo share of $q$, then

[30] Although the outcome is unique, there are multiple equilibria because different off-the-equilibrium-path beliefs will support this equilibrium. The fact that there is a unique outcome is surprising. Typically in bargaining games in which an informed bargainer (i.e., a bargainer with private information) can make offers, there is a multiplicity of equilibrium outcomes. For an excellent introduction to bargaining models, see Drew Fudenberg and Jean Tirole, *Game Theory* (Cambridge: MIT Press, 1991). A good survey is also found in John Kennan and Robert Wilson, "Bargaining with Private Information," *Journal of Economic Literature* 31 (March 1993).

[31] Robert Powell, "Bargaining in the Shadow of Power," *Games and Economic Behavior* (forthcoming).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

all types of $S_1$ that prefer $x$ to fighting accept $x$ and all other types attack. Given this response, the final step in the derivation of the equilibrium is to describe the satisfied states's optimal offer given its cost of fighting, its beliefs about $S_1$'s cost of fighting, and $S_1$'s response.

Step 1. A dissatisfied type will never reject an offer in order to make a counteroffer. It will either accept the offer on the table or fight.

A preliminary to establishing this claim is to put upper bounds on the satisfied state's offers and acceptances. Let $S_2$ be the satisfied state and suppose that $S_2$ is deciding what to offer $S_1$ at any point in the bargaining game. $S_2$ will have updated its initial beliefs about $S_1$'s cost in light of the offers $S_1$ has previously made. That is, $S_2$ will have revised its initial beliefs about $S_1$'s cost, which are represented by the probability distribution $F_1$, in light of $S_1$'s previous actions. These updated beliefs can also be represented by a new probability distribution.

Let $\hat{s}_1$ denote the toughest type of $S_1$ that $S_2$ believes it might be facing following a sequence of offers and counteroffers denoted by $h_t$. To put an upper bound on what the satisfied state might offer at any subsequent time, let $\hat{c}_1$ be $\hat{s}_1$'s cost of fighting. If $\hat{s}_1$ is a dissatisfied type, then the satisfied state $S_2$ will never offer more than what it takes to appease the toughest type that it might be facing. This is the smallest offer that ensures that $\hat{s}_1$ will not attack. Any higher offer would also ensure that $S_2$ would not be attacked but would mean a lower payoff if the offer were accepted. Formally, if $\hat{s}_1$ is dissatisfied, $S_2$ will never offer more than $\hat{x}$ where $\hat{x}$ satisfies $U_1(\hat{x}) = p - \hat{c}_1$. If $\hat{s}_1$ is satisfied, then $S_2$, although uncertain of the other state's exact cost of fighting, is sure that the other state is unwilling to use force to alter the status quo. In these circumstances, $S_2$ would never offer to revise the status quo in the other state's favor. In sum, $S_2$ would never offer more than the larger of $\hat{x}$ and $q$ at any time after the initial sequence of offers and counteroffers $h_t$.

To put an upper bound on the demands to which $S_2$ might accede following $h_t$, two cases must also be considered. First, suppose that the toughest type that $S_2$ might be facing, $\hat{s}_1$, is satisfied and therefore unwilling to use force to overturn the status quo. In this case, $S_2$ will find any threat to use force incredible. Hence, the largest demand that $S_2$ might accept in this case is a demand of $q$, which is really a "demand" to ratify the status quo. (Because $S_2$ is satisfied, it is also unwilling to revise the status quo forcibly.)

In the second case, $\hat{s}_1$ is dissatisfied. In these circumstances, if $S_2$ rejects the dissatisfied state's demand and counters with its maximal offer

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

of $\hat{x}$, this counter will be accepted immediately.[32] Given the immediate acceptance of $\hat{x}$, $S_2$'s payoff to rejecting a demand in order to counter with $\hat{x}$ is the payoff to having $1 - q$ for one more period, that is, the period in which it rejects the offer, and then having the share $1 - \hat{x}$ forever. This payoff is $U_2(1 - q) + \delta U_2(1 - \hat{x})/(1 - \delta)$. Thus, $S_2$ would never agree to a demand from $S_1$ that left $S_2$ with a less than $U_2(1 - q) + \delta U_2(1 - \hat{x})/(1 - \delta)$, for $S_2$ could do better by rejecting the demand and countering with $\hat{x}$. Accordingly, the only demands $y$ which $S_2$ might accept must satisfy $U_2(1 - y)/(1 - \delta) \geq U_2(1 - q) + \delta U_2(1 - \hat{x})/(1 - \delta)$. Solving for $y$ gives $y \leq \hat{y} = 1 - U_2^{-1}((1 - \delta)U_2(1 - q) + \delta U_2(1 - \hat{x}))$. $\hat{y}$, therefore, is an upper bound on the demands $S_2$ might accept when it believes that the toughest type it might be facing is $\hat{s}_1$.

Summarizing, $S_2$ will never offer more than the larger of $q$ and $\hat{x}$. Nor will $S_2$ agree to any demand giving the dissatisfied state more than the larger of $q$ and $\hat{y}$.

These upper bounds imply that no dissatisfied type of $S_1$ will reject an offer to make a counteroffer. This claim will be established by arguing by contradiction. That is, a dissatisfied type of $S_1$ will be assumed to reject an offer in order to make a counteroffer, and this assumption will be shown to lead to a contradiction.

Suppose there is an equilibrium in which, following a sequence of offers and counteroffers $h_t$ which ends in an offer of, say, $x$ from $S_2$, a dissatisfied type of $S_1$ rejects $x$ in order to make a counteroffer of some $y$. Let $\hat{s}_1$ denote the toughest type of $S_1$ that $S_2$ believes it might be facing after receiving the demand $y$, and let $\hat{c}_1$ be $\hat{s}_1$'s cost of fighting. In equilibrium, $\hat{s}_1$ must have been willing to make the counteroffer of $y$; otherwise $S_2$ would not believe that there is some chance that it might be facing $\hat{s}_1$. But $\hat{s}_1$ would be willing to counter with $y$ only if there were some chance that doing so would bring it at least as much as it could have had by simply attacking.

When considering whether to attack or counter with $y$, $\hat{s}_1$'s payoff to attacking is $W_1(0) = (p - \hat{c}_1)/(1 - \delta)$. As will be seen, the upper bounds on $S_2$'s offers and acceptances show that the payoff to countering is always less than $W_1(0)$. The fact that $\hat{s}_1$ could have done better by attacking rather than countering contradicts the assumption that $\hat{s}_1$ rejects an offer in equilibrium in order to make a counteroffer, for no type can

[32] To see that this offer will be accepted immediately, recall that $\hat{x}$ is designed to ensure that the dissatisfied state cannot do better than accepting $\hat{x}$ by fighting instead. In equilibrium, the dissatisfied state will never reject $\hat{x}$ in order to fight. And since $S_2$ will never offer more than $\hat{x}$, the dissatisfied state can gain nothing by holding out for a better offer. Indeed, the dissatisfied state will lose by not reaping the benefits from a favorable shift in the status quo from $q$ to $\hat{x}$ as soon as possible. Thus, the dissatisfied state will accept a counteroffer of $\hat{x}$ immediately.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

have a positive incentive to deviate from its equilibrium strategy. This contradiction will establish the claim made in step 1.

If $\hat{s}_1$ rejects an offer to make a counteroffer, the game could end in only one of three ways following the counter. First, the game could end in war in some future period. But the payoff to a dissatisfied type to living with the status quo for a while and then fighting is strictly less than the payoff to fighting now. In symbols, $W_1(t) < W_1(0)$ for $t \geq 1$. Thus, $\hat{s}_1$ strictly prefers not to counter if the game is eventually going to end in war.

The second way that the game could end is that $\hat{s}_1$ could ultimately accept an offer from $S_2$. But as shown above, $S_2$ never offers more than $\hat{x}$. Consequently, $\hat{s}_1$'s maximum payoff to countering with $y$ if the game subsequently ends with $\hat{s}_1$'s acceptance of an offer of $\hat{x}$ is $\hat{s}_1$'s payoff to living with the status quo for two periods—namely, the period in which $\hat{s}_1$ counters with $y$ and then the period in which $S_2$ rejects this offer in order to counter with $\hat{x}$—and then having $\hat{x}$ forever. In symbols, this payoff is $U_1(q) + \delta U_1(q) + \delta^2 U_1(1 - \hat{x})/(1 - \delta)$. But this payoff is less than $W_1(0) = (p - \hat{c}_1)/(1 - \delta)$, because $U_1(\hat{x}) = p - \hat{c}_1$ and, since $\hat{s}_1$ is dissatisfied, $p - \hat{c}_1 > U_1(q)$. Again, $\hat{s}_1$ does strictly better by fighting rather than countering if the game ends with $\hat{s}_1$'s ultimately accepting an offer from $S_2$.

The final way that the game could end is with $S_2$'s agreeing to a demand from $\hat{s}_1$. $\hat{s}_1$'s maximum payoff to this outcome occurs if $\hat{s}_1$ immediately counters with the maximal acceptable demand $\hat{y}$ and $S_2$ accepts. This would leave $\hat{s}_1$ with the payoff to living with the status quo for the period in which it rejects $x$ to counter with $\hat{y}$ and then having $\hat{y}$ forever. In symbols, $\hat{s}_1$'s payoff is $U_1(q) + \delta U_1(\hat{y})/(1 - \delta)$. This payoff is strictly less than $\hat{s}_1$'s payoff to fighting, $(p - \hat{c}_1)/(1 - \delta)$.[33] As before, $\hat{s}_1$ does strictly better by fighting rather than countering if the game ends with $S_2$ accepting $\hat{s}_1$'s demand.

In sum, $\hat{s}_1$ can increase its payoff by attacking rather than making a counteroffer regardless of how the game ends following $\hat{s}_1$'s counter. Accordingly, $\hat{s}_1$ would be able to increase its payoff by deviating from its equilibrium strategy if its equilibrium strategy were to reject an offer in order to make a counteroffer. This, however, is a contradiction because the definition of an equilibrium requires that no actor can improve its

[33] To see that $\hat{s}_1$'s payoff is strictly less that $W_1(0)$, note that the definition of $\hat{y}$ implies that $S_2$ is indifferent to accepting $\hat{y}$ now, which leaves $S_2$ with $1 - \hat{y}$ forever, and settling on $\hat{x}$ in the next period, which leaves $S_2$ with $1 - \hat{x}$ forever. Thus $U_2(1 - \hat{y})/(1 - \delta) = U_2(1 - q) + \delta U_2(1 - \hat{x})/(1 - \delta)$. But $S_2$ prefers the status quo share of $1 - q$ to what it will have after settling on either $1 - \hat{y}$ or $1 - \hat{x}$. That is, $1 - q > 1 - \hat{y}$. Given $1 - q > 1 - \hat{y}$, then the previous equality implies $1 - \hat{y} > 1 - \hat{x}$ or, equivalently, $\hat{x} > \hat{y}$. Finally, the fact that $\hat{x} > \hat{y} > q$ leaves $W_1(0) = (p - \hat{c}_1)/(1 - \delta) = U_1(\hat{x})/(1 - \delta) > U_1(q) + \delta U_1(\hat{y})/(1 - \delta)$.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

payoff by deviating from its equilibrium strategy. This contradiction thus establishes the claim that no dissatisfied type can reject an offer in equilibrium in order to make a counteroffer. If, moreover, no dissatisfied type will reject an offer to make a counter, then a dissatisfied type must choose one of the two remaining alternatives. It will either accept the offer on the table or attack, depending on which alternative yields the higher payoff.

Step 2. All satisfied types accept any offer larger than the status quo.

Assume as before that $S_1$ is the potentially dissatisfied state and that the satisfied state has offered to revise the status quo in favor of $S_1$. More formally, $S_2$ has offered $S_1$ a share $x$ where $x > q$ . As shown in step 1, a dissatisfied type of $S_1$ rejects $x$ if this type's payoff to fighting is higher than the payoff to accepting $x$ and accepts $x$ otherwise.

Now consider the decision facing a satisfied type of $S_1$, which is denoted by $\tilde{s}_1$. $\tilde{s}_1$ never attacks. To see that $\tilde{s}_1$ does not attack, note that the payoff to accepting $x$ is greater than the payoff to living with the status quo because $x > q$, and the payoff to living with the status quo is larger than the payoff to fighting because $\tilde{s}_1$ is satisfied. Thus, the payoff to accepting $x$ is greater than the payoff to fighting, and therefore $\tilde{s}_1$ will not attack.

Given that $\tilde{s}_1$ will not attack, its decision reduces to accepting $x$ or rejecting it in order to make a counteroffer. $\tilde{s}_1$ will accept $x$ because it offers the higher payoff. To calculate the payoff to rejecting $x$, recall that no dissatisfied type of $S_1$ will reject $x$ in order to make a counteroffer. If, therefore, $x$ is rejected, this rejection is in effect a signal to $S_2$ that it is facing only satisfied types of $S_1$. But as soon as $S_2$ becomes convinced that it is facing only satisfied types of $S_1$, it will find any threat from $S_1$ to use force to overturn the status quo inherently incredible. Thus, $S_2$ will never agree to revise the status quo in $S_1$'s favor. The status quo, therefore, will not be revised following the rejection of $x$. Hence, $\tilde{s}_1$'s payoff to rejecting $x$ is the payoff to living with the status quo. But $x > q$, so the payoff to agreeing to $x$ is higher than the payoff to living with the status quo. Accordingly, satisfied types of the potentially dissatisfied state will accept any offer $x > q$.

To see what satisfied types do if $S_2$ offers or, more aptly, demands a revision of the status quo in its favor, suppose $x < q$.[34] As before, all dissatisfied types of $S_1$ will either accept $x$ or fight, depending on which al-

[34] The analysis of the case in which $x = q$ is completely analogous.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ternative offers the higher payoff. Indeed, in the case in which $S_2$ offers less than the status quo, all dissatisfied types fight. (By definition, all dissatisfied types prefer fighting to the status quo, and, with $x < q$, the payoff to accepting $x$ is even less than the payoff to the status quo.) Because all dissatisfied types reject $x$ and fight, $S_2$ will infer once again that it is facing only satisfied types of $S_1$ if $x$ is countered. And, as just seen, once $S_2$ becomes convinced that it is facing only satisfied types, the status quo will not be changed. Thus, the choice confronting a satisfied type when $x < q$ is to attack, accept the offer, or reject it and live with the status quo. Of the three, a satisfied type prefers living with the status quo. The status quo payoff is higher than the payoff to accepting $x$ because $x < q$ and higher than the payoff to fighting because this type is satisfied. In sum, a satisfied type rejects $x$ in equilibrium if $x < q$ and it receives the payoff to living with the status quo.

Step 3: Specifying the satisfied state's optimal offers.

The first two steps in the derivation of the game's equilibrium describe how the types of the potentially dissatisfied state respond to an offer from the satisfied state. The satisfied state, in turn, will make its best offer in light of these responses and its beliefs about the dissatisfied state's costs. Let $s_2$ denote the type of $S_2$ with cost $c_2$. Then given its beliefs about the potentially dissatisfied state's costs, $s_2$ can determine the probability that $S_1$ will reject an offer of $x$ and attack. (Assume for now that $x > q$.) To wit, the type of $S_1$ with cost $c_1$ will reject $x$ and attack if this type is dissatisfied and prefers fighting to accepting $x$. In symbols, this type fights if $p - c_1 > U_1(x)$ or, equivalently, $p - U_1(x) > c_1$ . But, $S_2$'s beliefs about $S_1$'s costs can be used to calculate the probability that this cost is less than $p - U_1(x)$ and therefore that an offer of $x$ will lead to war. Let $R(x)$ denote the probability that $S_1$ will attack in response to $x$.

If a type of $S_1$ rejects $x > q$ and fights, $s_2$'s payoff will be $(1 - p - c_2)/(1 - \delta)$. If $x$ is accepted, its payoff is $U_2(1 - x)/(1 - \delta)$. (As shown above, $x$ will never be countered when $x > q$.) Thus, $s_2$'s expected payoff to offering $x$ is the payoff if $S_1$ attacks in reply to $x$ times the probability that $S_1$ attacks plus the payoff if $x$ is accepted times the probability that $x$ is accepted. Letting $P(x)$ denote this expected payoff leaves:

$$P(x) = \left(\frac{1 - p - c_2}{1 - \delta}\right) R(x) + \left(\frac{U_2(1 - x)}{1 - \delta}\right) (1 - R(x))$$

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

$s_2$, therefore, offers the value of $x$ that maximizes $P(x)$ subject to the condition that $x \geq q$.[35]

It is now straightforward to use the results of steps 1, 2, and 3 to describe the unique perfect Bayesian equilibrium outcome of the bargaining game. Suppose that the game begins with the satisfied state's making the initial offer to the potentially dissatisfied state. The potentially dissatisfied state will respond to this initial offer as outlined above: dissatisfied types will accept it or fight, depending on which alternative yields the higher payoff, and satisfied types will accept if the offer is more than the status quo and will reject if it is less than the status quo. The satisfied state will then use its initial beliefs about the potentially dissatisfied state's costs to determine the probability that the potentially dissatisfied state will respond to a particular offer by attacking. And given these probabilities, the satisfied state will make its optimal offer, which is the value of $x$ that maximizes $P(x)$ for $x \geq q$ and where the probability that an initial offer of $x$ is rejected is $R(x) = F_1(p - U_1(x))$.[36] The probability that the bargaining will end in war is, in equilibrium, simply the probability that the potentially dissatisfied state will reply to this optimal initial offer by attacking.[37]

## Stability and the Distribution of Power

The equilibrium of the bargaining model makes it possible to calculate the probability of war as a function of the distribution of power. This section calculates this relation in a specific case and then compares these results to the expectations of the balance-of-power and preponderance-of-power schools and to other formal work. The section also offers a possible explanation for the equivocal results of empirical efforts to determine the relation between stability and the distribution of power and briefly considers some of the difficulties of estimating this relation empirically. Finally, the section discusses the relation between the probability of war and the distribution of power in more general cases. As in the specific case analyzed in detail here, the expectations of

[35] The expression for $P(x)$ was derived on the basis of the assumption that $x > q$. If $x \leq q$, $s_2$'s expected payoff to offering $x$ is $P(q)$. Accordingly, $s_2$ is indifferent to offering any $x \leq q$ and it will suffice to maximize $P$ over the range $x \geq q$.

[36] $s_1$ rejects $x$ if $p - c_1 > U_1(x)$ or $p - U_1(x) > c_1$. Given that $c_1$ is distributed according to the cumulative distribution function $F_1$, the probability that $c_1$ is less than $p - U_1(x)$ is $F_1(p - U_1(x))$.

[37] Although cumbersome to show, the probability that the bargaining will end in war is essentially the same regardless of whether the satisfied state or the potentially dissatisfied state makes the initial offer. See Powell (fn. 31) for the details.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

both the balance-of-power and the preponderance-of-power schools fail to hold in these more general cases.

To simplify the analysis, assume that the states are risk neutral and that each believes the other's cost of fighting is uniformly distributed between zero and one. Risk neutrality and the previous normalizations of the states' utility functions imply that $S_1$'s and $S_2$'s utilities for the division $(x, 1 - x)$ are simply $x$ and $1 - x$, respectively.

The probability of war turns out to be a simple function of the disparity between the distribution of power and the status quo distribution of territory. More specifically, the absolute value of the difference between the distribution of power and the status quo distribution of territory, $|p - q|$, is a measure of the disparity between these two distributions. Letting $\Pi(p,q)$ denote the probability of war as a function of $p$ and $q$, the appendix then shows:

$$\Pi(p,q) = \begin{cases} |p-q| - |p-q|^2 & \text{if} \quad |p-q| \leq 1/2 \\ 1/4 & \text{if} \quad |p-q| \geq 1/2 \end{cases}$$

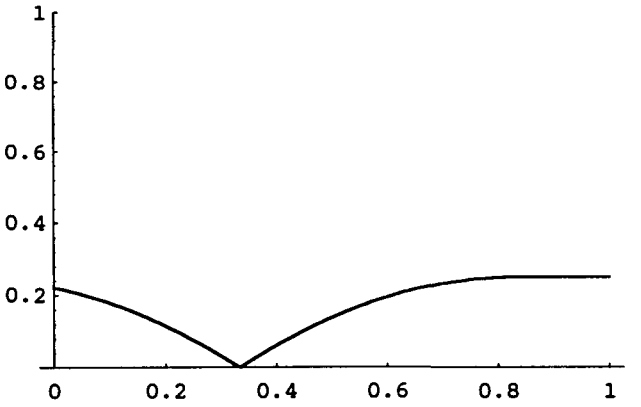
These results seem quite intuitive. When the distribution of power mirrors the status quo, that is, when $p = q$, neither state expects to gain by using force to revise the status quo. The probability of war in this case is zero. In symbols, $\Pi(p,q) = 0$ when $p = q$. As the disparity between the distribution of power and the status quo distribution grows, the probability of war rises until it levels off at 1/4.[38]

Figure 2 plots the relation between the probability of war and the distribution of power for three different values of the status quo distribution. $S_1$'s status quo share of territory is 1/3 if $q = 1/3$; 1/2 if $q = 1/2$; and 2/3 if $q = 2/3$. These results clearly contradict the expectations of both the balance-of-power and the preponderance-of-power schools. As illustrated in Figure 3a, the preponderance-of-power school expects the probability of war to be smallest when $S_1$ or $S_2$ is predominant (that is, when $p$ is large or small) and to increase as the distribution of power becomes more even (that is, as $p$ approaches 1/2). But in the case analyzed here, the probability of war is smallest at $p = q$ and generally largest when one of the states is preponderant.

[38] The specific value of 1/4 at which the function levels off is a result of the particular assumption that the states' costs are uniformly distributed between the bounds of zero and one. Different assumptions about these bounds would cause the function to level off at a different value.

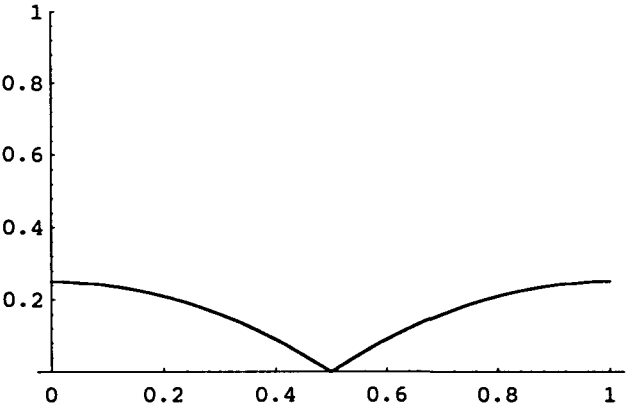
LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

q = 1/3



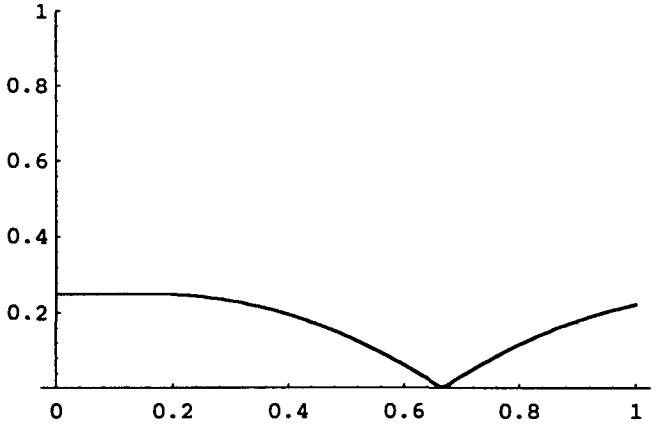

2a

q = 1/2




2b

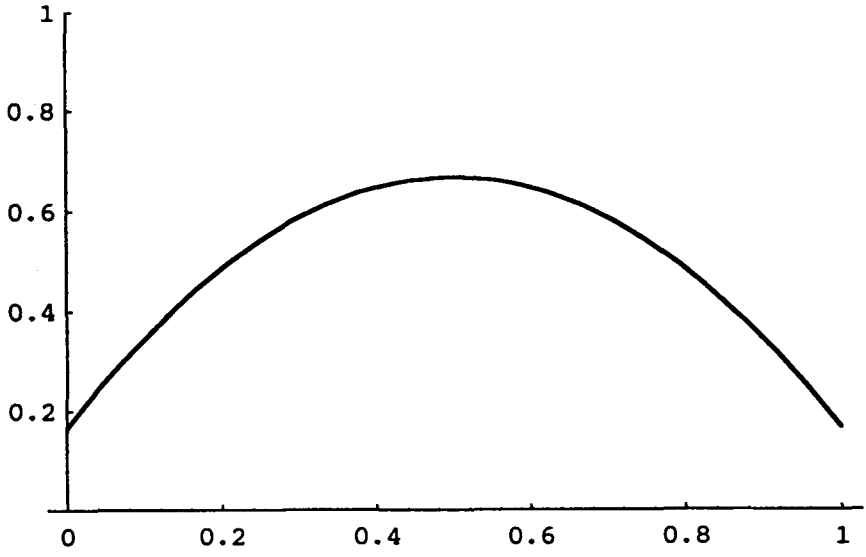
q = 2/3



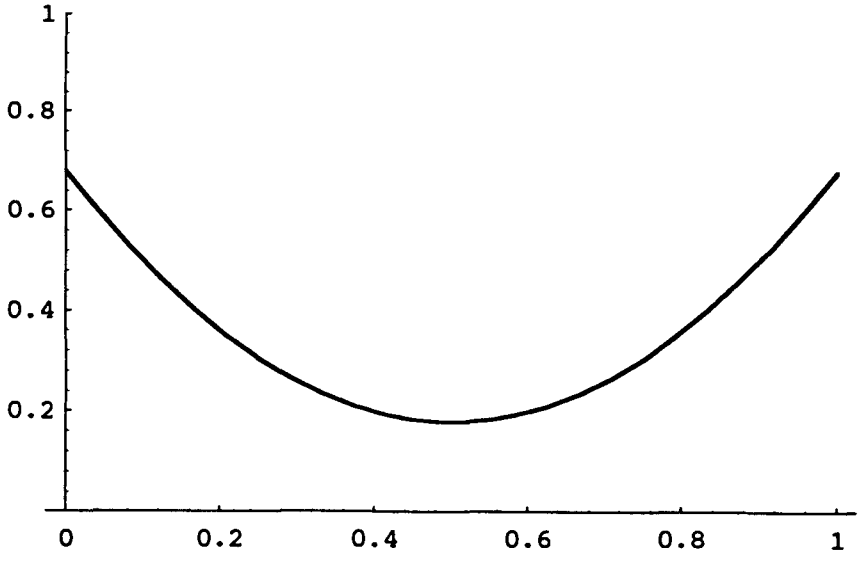

2c

FIGURE 2
THE PROBABILITY OF WAR AND THE DISTRIBUTION OF POWER

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED




(a) PREPONDERANCE OF POWER




(b) BALANCE OF POWER

FIGURE 3
EXPECTATIONS OF THE TWO SCHOOLS

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Figure 3b illustrates the balance-of-power school's expectations. The probability of war is smallest when there is a roughly even distribution of power ($p$ is approximately 1/2) and increases as the distribution of power becomes skewed. These expectations correspond to the formal results only in the special circumstance in which the status quo division is even ($q = 1/2$). When the status quo division is uneven, as in Figure 2a and 2c, the probability of war in the model is smallest when the distribution of power mirrors the uneven status quo division and not, as the balance-of-power school asserts, when the distribution is even.

The present analysis also complements and qualifies the results of other formal analyses of the relation between stability and the distribution of power. Bueno de Mesquita and Lalman, for example, study a model in which two states bargain about revising the status quo.[39] In their game each state has the opportunity to make a single demand of the other state. After both states have made their demands, each state decides whether or not to use force to secure its demand. In one version of this game Bueno de Mesquita and Lalman assume that the size of each state's demand is determined outside the model. That is, the amount each state demands is simply one of the exogenously specified initial conditions of the model. In this version of Bueno de Mesquita and Lalman's model, the size of a state's demand is not determined as part of a state's equilibrium strategy. A state does not determine how much it demands by balancing the risk of war against the chance of agreeing on a more favorable settlement. The justification for assuming the states' demands to be exogenous is that these demands are "determined by internal political rules, procedures, norms, and considerations and may or may not be attuned to foreign policy considerations."[40] With the size of the states' demands determined outside the model, Bueno de Mesquita and Lalman find that "dissatisfaction with the status quo is entirely unrelated to the likelihood of war."[41]

The present analysis focuses specifically on how a state balances the greater risk that a larger demand will lead to war against the higher payoff the state will obtain if this larger demand is accepted. This focus requires a model in which the states determine the sizes of their de-

[39] Bueno de Mesquita and Lalman (fn. 2, 1992).

[40] Ibid., 41.

[41] Ibid., 190. In a second version of their game, Bueno de Mesquita and Lalman let the state's demands be determined as part of their equilibrium strategies. But this game has complete information. The combination of endogenous demands and complete information means that the probability of war is zero in their model—as well as in the model analyzed above—regardless of the distribution of power. Bueno de Mesquita and Lalman do not examine the case in which there are both endogenous demands and incomplete information.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

mands as part of their equilibrium strategies. The game examined here satisfies this requirement. The probability of war in the present game, unlike in Bueno de Mesquita and Lalman's model, is closely related to the level of dissatisfaction with the status quo.[42] The larger the level of dissatisfaction in the case above, that is, the larger the disparity $|p - q|$, the more likely war.[43]

Fearon also considers the relation between the probability of war and the distribution of power. He studies a game in which one state makes a take-it-or-leave-it offer after which a second state must then either accept this offer or attack. By assumption, this second state cannot make a counteroffer. The size of the state's demand in Fearon's model is determined as part of the state's equilibrium strategy, and he finds that the probability of war is "*completely insensitive*" to the distribution of power.[44]

The current model complements Fearon's formulation. He is studying a stylized situation in which one state presents another state with an ultimatum in the form of a military fait accompli. This fait accompli establishes a new distribution that will become the new international status quo unless the second state goes to war to reverse it.[45] In the stylized situation modeled in this essay, two states are bargaining about revising the status quo and have the opportunity to make offers and counteroffers. There are, however, no military faits accomplis: any use of force to revise the status quo is assumed to lead directly to war. In these circumstances the probability of war is sensitive to the distribution of power and, in particular, to the disparity between the distribution of power and the status quo distribution of territory.

The present analysis provides a possible explanation of the equivocal findings of empirical efforts to determine the relation between stability and the distribution of power. Empirical research has yielded at least three different findings about an even distribution: that it is more stable than a preponderance of power,[46] that it is less stable than a preponderance of power,[47] and, depending on whether one looked at the nineteenth or the twentieth century, that it is either more or less stable.[48]

[42] Bueno de Mesquita and Lalman (fn. 2, 1992), 190.

[43] Strictly speaking, the probability of war increases as $|p - q|$ increases only as long as $|p - q| < 1/2$. After this, the probability of war levels off.

[44] Fearon (fn. 4), 20.

[45] Ibid., 15.

[46] Siverson and Tennefoss (fn. 2).

[47] Kim (fn. 2, 1992); and Moul (fn. 2).

[48] Singer, Bremer, and Stuckey (fn. 2).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Other work has found no significant relation between stability and the distribution of power.[49]

The equilibrium of the bargaining game shows that the probability of war depends on both the distribution of power and the status quo distribution. Thus, any attempt to assess the relation between the probability of war and the distribution of power should control for the status quo. Failing to do so will generally lead to biased estimates if, as might be expected, the distribution of power and the status quo distribution are correlated. But empirical efforts to estimate this relation have generally not controlled for the status quo, and this omission may partially account for the equivocal empirical results.[50]

Finally, it is important to ask about the generality of these results. Do the findings hold only in the specific example considered here in which the states were assumed to be risk neutral and to believe that each other's cost or willingness to use force was uniformly distributed? Or do the results also hold in more general conditions? The central finding that the probability of war is at a minimum when the distribution of power mirrors the status quo distribution is quite robust. It holds as long as the states are risk neutral or risk averse, regardless of the particular shapes of their utility functions or of the particular shapes of the probability distributions representing their beliefs.[51] Thus, the model contradicts the expectations of the balance-of-power and preponderance-of-power schools as long as the states are risk neutral or risk averse.[52]

One might also wonder if this result holds if the uncertainty sur-

[49] Maoz (fn. 2); and Bueno de Mesquita and Lalman (fn. 2, 1992).

[50] Unfortunately, the theoretical results derived here, while indicating the importance of controlling for the status quo, do not identify a means of doing so. The basic problem is to find a way of measuring a state's utility for the status quo. Bueno de Mesquita and Lalman's (fn. 2, 1992) measure of this utility may offer a start in this direction, but their current formulation is inadequate. If the states are risk neutral as in the example above, then Bueno de Mesquita and Lalman's measure reduces to assuming that the status quo distribution is constant in all cases. In terms of the example above, they are in effect assuming that $q$ always equals 1/2. (To obtain $q = 1/2$, assume the state is risk neutral by taking $r_A = 1$ in equation A1.3 in Bueno de Mesquita and Lalman (fn. 2, 1992), 294, and normalize the state's utility to be one if it obtains everything it demands and zero if the other state obtains everything it demands by setting $U^A(\Delta_A) = 1$ and $U^A(\Delta_B) = 0$ .) Controlling for the status quo, however, requires the status quo to be treated as a variable across cases, and it is unclear how to do this with their measure as it is currently formulated.

[51] To see this, suppose that the distribution of power closely mirrors the status quo distribution of territory in that $|p - q|$ is less than the minimium of the lowest possible costs of fighting, i.e., the minimum of $\underline{c}_1$ and $\underline{c}_2$. Then, $p - q \leq \underline{c}_1$ and $q - p \leq \underline{c}_2$. These inequalities and the concavity of $U_1$ and $U_2$ imply $p - \underline{c}_1 \leq q \leq U_1(q)$ and $1 - p - \underline{c}_2 \leq 1 - q \leq U_2(1 - q)$. Thus, both $S_1$ and $S_2$ are satisfied, and the probability of war is zero.

[52] The case of risk-acceptant states introduces nonconvexities and technical difficulties, and the analysis of this case remains a task for future work.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

rounding the states' willingness to use force varies with shifts in the distribution of power. More specifically, the costs of fighting in the example examined here are always uniformly distributed between 0 and 1 regardless of the distribution of power. But what would happen if the expected cost and uncertainty about a state's willingness to use force declined as that state became more powerful?[53]

This question requires a two-part response. First, the question itself takes the analysis beyond the balance-of-power and predominance-of-power schools, as neither school bases its argument on the subtleties implicit in this question. Second, the model provides a partial answer to this question. The probability of war is still zero as long as the status quo distribution of benefits mirrors the distribution of power.[54] Once again, the expectations of the balance-of-power and preponderance-of-power schools fail to hold.[55]

## Conclusion

The relation between the distribution of power and the probability of war is an important and long-debated problem in international relations theory. The balance-of-power school argues that an even distribution of power brings greater stability, while the preponderance-of-power school argues that a preponderance brings greater stability. These opposing claims have been examined in the context of an infinite-horizon bargaining game in which two states alternate making offers about how to revise the international status quo. The bargaining continues until the states agree on a revision or until one of them becomes sufficiently pessimistic about the prospects of reaching a mutually agreeable settlement that it resorts to force in an attempt to impose a new settlement. Contradicting the expectations of both the balance-of-power and preponderance-of-power schools, the probability of war in the model is smallest when the distribution of power mirrors the status quo distribution.

[53] More formally, suppose that the distributions of cost $F_1$ and $F_2$ were also a function of $p$ and that the mean and variance of $F_1$ decrease in $p$ while the mean and variance of $F_2$ decrease in $1 - p$.

[54] Even if $F_1$ and $F_2$ depend on $p$, the argument in footnote 26 goes through with only minor modification.

[55] The model's answer is only partial because the shape of the function relating the probability of war to the distribution of power, while always zero when $p = q$, is likely to depend on the states' utility functions and on the functional forms of the probability distributions representing their beliefs.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## APPENDIX

There are two cases to consider in calculating the probability of war as a function of the distribution of power. Suppose, first, that $p > q$. Then $S_1$ is the potentially dissatisfied state, because the expected payoff to fighting for the type of $S_1$ with the lowest cost of fighting is strictly greater than its status quo payoff: $p - c_1 = p - 0 > q$. Then, as shown above, the probability of war in the bargaining game is the probability that the dissatisfied state attacks in response to the satisfied state's optimal initial offer.

To calculate this probability, $S_2$'s optimal initial offer must first be determined. Suppose $S_2$ offers $x$ to $S_1$. A dissatisfied type $s_1$ of $S_1$ with cost $c_1$ will reject this offer and attack if its payoff to fighting is higher than its payoff to accepting. That is, $s_1$ attacks if $p - c_1 > x$ or, equivalently, if $p - x > c_1$. Thus, the probability that $S_1$ will attack in response to an offer of $x$ is the probability that $S_1$'s cost is less than $p - x$. Given that $S_1$'s costs of fighting are uniformly distributed between 0 and 1, the probability that $S_1$'s cost is less than $p - x$ is just $p - x$. Consequently, $S_2$'s expected payoff to offering $x$, which will be denoted by $P(x)$, is its payoff to fighting times the probability that $S_1$ will attack plus the payoff if $S_1$ accepts $x$ times the probability that $S_1$ will accept $x$. In symbols,

$$P(x) = \frac{1 - p - c_2}{1 - \delta}(p - x) + \frac{(1 - x)}{1 - \delta}(1 - (p - x))$$

if $S_2$'s offer is between $q$ and $p$. If $S_2$ offers more than $p$, then even the dissatisfied state with the lowest cost of fighting will prefer to accept the offer to fighting. Consequently, the probability that an offer of $x > p$ will be rejected is 0. $S_2$'s payoff to offering $x$ in this case reduces to $(1 - x)/(1 - \delta)$. If $S_2$ offers $x < q$, then all dissatisfied types fight and all other types reject the demand which leave the status quo unchanged. $S_2$'s payoff is:

$$\frac{1 - p - c_2}{1 - \delta}(p - q) + \frac{(1 - q)}{1 - \delta}(1 - (p - q)).$$

$S_2$'s optimal offer is the value of $x$ that maximizes its expected payoff. To describe the solution to this maximization problem, set the derivative of $P(x)$ equal to zero and let $x^*(c_2)$ denote the solution to this equa-

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tion. This leaves $x^*_1(c_2) = p - (1 - c_2)/2$. Then the optimal offer of the type of $S_2$ with cost $c_2$ is $x^*(c_2)$ as long as $x^*(c_2) \geq q$. $S_2$'s optimal offer is $q$ if $x^*(c_2) < q$.

Now that the equilibrium offers have been specified, the probability of breakdown can be calculated. Let $\pi(c_2)$ be the probability that the type of $S_2$ with cost $c_2$ will be attacked. If $x^*(c_2) < q$ for this type, then this type will offer $q$. The probability that the dissatisfied state will attack in response to this offer is the probability that the cost of fighting $c_1$ is less than $p - q$ which, given the uniform distribution of costs, is simply $p - q$. Thus, $\pi(c_2) = p - q$ for all types of $S_2$ for which $x^*(c_2) < q$ or, equivalently, for all types of $S_2$ for which $c_2 < 1 - 2(p - q)$.

If $x^*(c_2) \geq q$ for a type of $S_2$, then this type will offer $x^*(c_2)$. The probability that the dissatisfied state attacks in response to this offer is $p - x^*(c_2) = p - (p - (1 - c_2)/2) = (1 - c_2)/2$. Thus, $\pi(c_2) = (1 - c_2)/2$ whenever $x^*(c_2) \geq q$ or $c_2 \geq 1 - 2(p - q)$.

$\pi(c_2)$ specifies the probability that the particular type of $S_2$ with cost $c_2$ will fight. But from the perspective of an outside observer, as well as from that of $S_1$, $S_2$'s cost is uncertain. Thus the probability of war is the expected value of $\pi(c_2)$. Letting $\Pi(p,q)$ denote this expected value, then:

$$\Pi(p,q) = \int_0^1 \pi(c_2)dc_2$$

$$\Pi(p,q) = \begin{cases} (p - q) - (p - q)^2 & \text{if} \quad 0 \leq p - q \leq 1/2 \\ 1/4 & \text{if} \quad 1/2 \leq p - q \end{cases}$$

$\Pi(p, q)$ describes the relation between the probability of breakdown and the distribution of power if $p > q$ and, consequently, $S_1$ is the dissatisfied state. If $p < q$, then $S_2$ is the dissatisfied state and the relation between stability and the probability of war must be determined anew. Fortunately, the symmetry of the problem makes it easy to find this relation in this second case. Let $p' = 1 - p$ and $q' = 1 - q$. Then $p < q$ implies $p' > q'$. Moreover, $p'$ now measures the probability that the dissatisfied state will prevail and $q'$ measures the dissatisfied state's status quo payoff just as $p$ and $q$ did in the first case where $p > q$. The symmetry of the example then ensures that the probability of breakdown if $p <$

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

$q$ is given by $\Pi(p', q')$. But $\Pi(p', q')$ is just $\Pi(1 - p, 1 - q)$ which in turn equals $(q - p)(1 - (q - p))$ if $1 - 2(q - p) \geq 0$ and 1 /4 if $1 - 2(p - q) < 0$.

Combining these results leaves:

$$\Pi(p, q) = \begin{cases} |p - q| - (p - q)^2 & \text{if} \quad |p - q| \leq 1/2 \\ 1/4 & \text{if} \quad |p - q| \geq 1/2 \end{cases}$$

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

*Review Article*

# PHOENIX RISEN
## The Resurrection of Global Finance

By BENJAMIN J. COHEN*

John B. Goodman. *Monetary Sovereignty: The Politics of Central Banking in Western Europe*. Ithaca, N.Y.: Cornell University Press, 1992, 238 pp.
Eric Helleiner. *States and the Reemergence of Global Finance: From Bretton Woods to the 1990s*. Ithaca, N.Y.: Cornell University Press, 1994, 244 pp.
Ethan B. Kapstein. *Governing the Global Economy: International Finance and the State*. Cambridge: Harvard University Press, 1994, 224 pp.
Paulette Kurzer. *Business and Banking: Political Change and Economic Integration in Western Europe*. Ithaca, N.Y.: Cornell University Press, 1993, 261 pp.
Andrew C. Sobel. *Domestic Choices, International Markets: Dismantling National Barriers and Liberalizing Securities Markets*. Ann Arbor: University of Michigan Press, 1994, 211 pp.

OF all the many changes of the world economy in recent decades, few have been nearly so dramatic as the resurrection of global finance. A half century ago, after the ravages of the Great Depression and World War II, financial markets everywhere—with the notable exception of the United States—were generally weak, insular, and strictly controlled, reduced from their previously central role in international economic relations to offer little more than a negligible amount of trade financing. Starting in the late 1950s, however, private lending and investment once again began to gather momentum, generating a phenomenal growth of cross-border capital flows and an increasingly close integration of domestic financial markets. Like a phoenix risen from the ashes, global finance took flight and soared to new heights of power and influence in the affairs of nations.

How can we explain the remarkable globalization of financial markets of recent years, and what are its economic and political implica-

* I am indebted to David Andrews, Joe Grieco, Miles Kahler, Helen Milner, and Louis Pauly for helpful comments and suggestions. The able assistance of Kathleen Collihan is also gratefully acknowledged.

*World Politics* 48 (January 1996), 268–96

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tions? Such questions have lately spawned a veritable cottage industry of popular commentary, some of it frankly sensationalist if not downright alarmist in tone.[1] Even otherwise levelheaded scholars have at times allowed themselves to be carried away by gnawing fears of instability and chaos.[2] A new generation of political economists, however, is beginning to focus its attention on the phenomenon, casting the cool eye of objective analysis on both the causes and consequences of financial globalization. A survey of this emerging literature, including the five books under review here,[3] suggests just how much can be learned about such a topical issue from more serious and substantive scholarship.

The aim of this article is both to summarize present understanding of the political economy of global finance and to identify key elements of an agenda for future research. For our purposes, global finance is assumed to encompass all types of cross-border portfolio-type transactions—borrowing and lending, trading of currencies or other financial claims, and the provision of commerical banking or other financial services. It also includes capital flows associated with foreign direct investment—transactions involving significant control of producing enterprises. Financial globalization (or internationalization) refers to the broad integration of national markets associated with both innovation and deregulation in the postwar era and is manifested by increasing movements of capital across national frontiers. The more alternative assets are closely regarded as substitutes for one another, the higher the degree of capital mobility.

[1] See, e.g., Howard M. Wachtel, *The Money Mandarins: The Making of a New Supranational Economic Order* (Armonk, N.Y.: M. E. Sharpe, 1990); Richard B. McKenzie and Dwight R. Lee, *Quicksilver Capital: How the Rapid Movement of Wealth Has Changed the World* (New York: Free Press, 1991); Joel Kurtzman, *The Death of Money: How the Electronic Economy Has Destabilized the World's Markets and Created Financial Chaos* (New York: Simon and Schuster, 1993); Gregory J. Millman, *The Vandals' Crown: How Rebel Currency Traders Overthrew the World's Central Banks* (New York: Free Press, 1995); and Steven Solomon, *The Confidence Game: How Unelected Central Bankers Are Governing the Changed Global Economy* (New York: Simon and Schuster, 1995).

[2] Susan Strange, *Casino Capitalism* (New York: Basil Blackwell, 1986).

[3] Other recent contributions of note include Stephen R. Gill and David Law, "Global Hegemony and the Structural Power of Capital," *International Studies Quarterly* 33 (December 1989); Geoffrey R. D. Underhill, "Markets beyond Politics? The State and the Internationalisation of Financial Markets," *European Journal of Political Research* 19 (March–April 1991); Tariq Banuri and Juliet B. Schor, eds., *Financial Openness and National Autonomy: Opportunities and Constraints* (Oxford: Clarendon Press, 1992); John B. Goodman and Louis W. Pauly, "The Obsolescence of Capital Controls? Economic Management in an Age of Global Markets," *World Politics* 46 (October 1993); Philip G. Cerny, ed., *Finance and World Politics* (Aldershot, England: Edward Elgar, 1993); David M. Andrews, "Capital Mobility and State Autonomy: Toward a Structural Theory of International Monetary Relations," *International Studies Quarterly* 38 (June 1994); Stuart Corbridge, Nigel Thrift, and Ron Martin, eds., *Money, Power and Space* (Cambridge: Basil Blackwell, 1994); and Eric Helleiner, ed., "The World of Money: The Political Economy of International Capital Mobility," *Policy Sciences* 27, no. 4 (1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

The scope of financial globalization should not be exaggerated. As much as capital flows have grown, it is still premature to speak of a single, world financial market. In the words of Jeffry Frieden, "International investment is by no means yet a seamless web."[4] Careful econometric studies demonstrate that even for the most liquid of monetary assets, capital mobility remains imperfect because of inherent country and currency risks.[5] Market segmentation persists, both within states (among different sectors) and between them. Debt instruments are less transferable than cash, long-term claims are less substitutable than short-term, and equity markets are less integrated still. The scope of globalization, however, also should not be underestimated. Though frictions between markets remain, they are far fewer and weaker today than they used to be; both domestically and internationally, functional and institutional linkages have greatly increased. The trend in finance has been toward ever higher levels of global interdependence.

This survey will begin with a brief synopsis of the five books under review, highlighting the core concerns and conclusions of each. Though individually quite diverse, the five as a group constitute a reasonably representative sample of work currently under way in this specialized subfield of international political economy. The following sections will then take up three of the most critical questions posed by the globalization of financial markets: How did it happen? What does it mean for economic performance or policy? What can governments do about it? Answers vary considerably, suggesting much room for further research, particularly on implications for the central political-economy dialectic between politics and markets. At a minimum, financial globalization has put governments distinctly on the defensive, eroding much of the authority of the contemporary sovereign state. At a maximum, it may have irreversibly altered the meaning of geography in the world economy today. The phoenix has risen. Does it also rule the roost?

[4] Jeffry A. Frieden, "Invested Interests: The Politics of National Economic Policies in a World of Global Finance," *International Organization* 45 (Autumn 1991), 429.

[5] See, e.g., Jeffrey A. Frankel, *On Exchange Rates* (Cambridge: MIT Press, 1993), chap. 2; Barry P. Bosworth, *Saving and Investment in a Global Economy* (Washington, D.C.: Brookings Institution, 1993), chap. 1; William F. Shepherd, *International Financial Integration: History, Theory and Applications in OECD Countries* (Brookfield, Vt.: Ashgate Publishing, 1994), chap. 4; Richard J. Herring and Robert E. Litan, *Financial Regulation in the Global Economy* (Washington, D.C.: Brookings Institution, 1995), chap. 2; and Atish R. Ghosh, "International Capital Mobility amongst the Major Industrialised Countries: Too Little or Too Much?" *Economic Journal* 105 (January 1995). Country (or political) risk refers to the possibility that assets may be treated differently by different sovereign governments; currency (or foreign-exchange) risk, to the possibility of exchange-rate movements that may alter the rate of return on investments. For some useful discussion, see Richard J. Herring, ed., *Managing International Risk* (Cambridge: Cambridge University Press, 1983).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## The Globalization of Finance

Recent scholarship, as indicated, has addressed both the causes and the consequences of financial globalization. The question of causes is taken up by Eric Helleiner and Andrew Sobel in two admirably detailed historical studies. Both agree on the key role played by states, particularly the major industrial powers, in deregulating domestic markets and liberalizing external controls. They disagree sharply, however, on how to explain the policies they observe.

For Helleiner, the story lies in a combination of structural and ideational factors. At the systemic level, "competitive deregulation" by governments maneuvering unilaterally to attract the business of mobile financial traders was reinforced as early as the 1960s by policy initiatives from the two leading financial powers of the day, the United States and Britain, both with a strong interest in promoting a more open international order. At the cognitive level, an ideological shift from postwar Keynesianism to a neoclassical or neoliberal policy framework gained strength from the preexistence of a sophisticated epistemic community of central bankers based around the Bank for International Settlements (BIS). The bulk of Helleiner's discussion is an account of the role played by each of these factors in the resurrection of global finance over the postwar period.

For Sobel, by contrast, the process is best explained by purely domestic considerations—competition between organized interests within national political economies that has spilled over to affect the international environment. Focusing specifically on recent developments in the securities markets of Britain, Japan, and the United States, Sobel rejects structural or ideational interpretations of globalization, which he labels "outside-in" explanations. "In these explanations, the primary stimulus motivating change arises outside the domestic political economy, but compels changes that impact the domestic political economy" (p. 15). Sobel prefers instead an alternative "inside-out" explanation, which he defends with extensive evidence of persistent national distinctions and "home bias" in bond and equity markets. "Paradoxical inconsistencies in behavior across the three markets pose dilemmas for outside-in explanations" (p. 15).[6] Incomplete convergence, he argues, suggests that "the international outcome is

[6] Though unacknowledged by Sobel, use of the terms "outside-in" and "inside-out" to describe alternative approaches to the study of international relations was pioneered by Kenneth Waltz. See Waltz, *Theory of World Politics* (Reading, Mass.: Addison-Wesley, 1979), 63.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

solidly rooted in domestic policy dilemmas and distributional debates" (p. 19).[7]

Consequences rather than causes are the principal concerns of the remaining three authors, again with strikingly divergent results. All three concur that financial globalization has indeed put government on the defensive, but they part company on what policymakers can do about it.

A fairly pessimistic view is represented by Paulette Kurzer, who sees rather little scope for effective state responses to global finance. Kurzer's densely textured comparative study examines the fate in the 1980s of tripartite distributive arrangements between business, labor, and government in four small European democracies: Austria, Belgium, the Netherlands, and Sweden. In all four countries, traditional policies of "social concertation" have recently been abandoned. The timing of these changes varied across the countries, which may be explained by differences in such factors as business preferences, administrative rulings, and the historical stance of foreign economic policies. But the overall outcome ultimately was the same in each and may be attributed, Kurzer insists, to a single cause—financial globalization: "As business and finance became more mobile, their power resources increased, and those of labor decreased. . . . [T]he greater mobility of capital and deepening financial integration corroded social concertation" (p. viii). As a result, Kurzer concludes grimly, "governments have lost the ability to carve out national economic strategies and to sustain social accords" (p. viii).

An alternative, rather more sanguine view is proposed by Ethan Kapstein in an informed and insightful survey of regulatory responses to the internationalization of commercial banking over the postwar period. Focusing in particular on prudential and supervisory agreements that have been negotiated by major central banks through the BIS, Kapstein identifies a formula, "international cooperation based on home country control," which, in his view, has enabled governments to mount an effective response to the challenges of financial globalization. Though imperfections remain, he argues, a workable framework for governing global financial markets has been created and may even suggest a "generic policy solution" to the conflicting demands of systemic and societal forces in other issue-areas as well: "International coopera-

[7] For parallel arguments concerning the critical role of domestic politics in shaping distinctive national patterns of financial liberalization, see Louis W. Pauly, *Opening Financial Markets: Banking Politics on the Pacific Rim* (Ithaca, N.Y.: Cornell University Press, 1988); Frances McCall Rosenbluth, *Financial Politics in Contemporary Japan* (Ithaca, N.Y.: Cornell University Press, 1989); and Sylvia Maxfield, *Governing Capital: International Finance and Mexican Politics* (Ithaca, N.Y.: Cornell University Press, 1990).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

tion based on home country control provides a way for states to enjoy the benefits of interdependence while maintaining national responsibility for the sector in question" (p. 180).

Finally, a third view is offered by John Goodman in a highly instructive comparative analysis of central banking practices in three big West European economies: France, Germany, and Italy. Goodman's primary concern is with the role played by institutional differences, particularly differences in the degree of central-bank independence that "govern the extent to which domestic political pressures influence national monetary policy" (p. 221). His discussion, however, is distinguished from most institutional studies in its assumption not of a closed economy but rather a context of deepening financial interdependence. The globalization of finance, he argues, drives states voluntarily to limit their own monetary autonomy by means of cooperation—in Europe, his specific area of focus, up to and including the possible creation of a full monetary union. Authority may be lost at the national level but might be regained through a convergence of policies at a higher level. In effect, therefore, Goodman strikes a middle ground between Kurzer's pessimism and Kapstein's optimism. Governments have not necessarily lost the ability to carve out effective economic strategies, but cooperation based on home country control is unlikely to prove sufficient. If they are to be successful, states must do the job collectively.

## How Did It Happen?

As the contrasting views of Helleiner and Sobel suggest, little consensus exists concerning the causes of financial globalization. Not that this is particularly surprising. Historical interpretation is never easy, even in a field as well documented as international finance. The discord, however, is significant insofar as the past may be assumed to have some impact on the course of events in the future. One does not have to hold a particularly rigid view of path dependency to recognize the extent to which tomorrow's choices may be delimited by yesterday's actions. An understanding of antecedents does matter.

Competing hypotheses may be categorized in any number of ways. Helleiner contrasts two classes of causal interpretation—those explanations that see globalization as a direct product of "unstoppable technological and market forces [that] discount the role played by states" (p. 1); and those, like his own, that stress instead the central role of government policies. Sobel, on the other hand, distinguishes three types of interpretation. Two are his so-called outside-in explanations, one posit-

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ing change "as a response to systemic conditions that affect all states" (p. 14), including technological developments and ideological shifts; the second viewing liberalization and internationalization as "a foreign policy outcome" (p. 15) reflecting the direct exercise of state influence. The third is his preferred inside-out interpretation. Yet another classification is proposed by Philip Cerny, a frequent contributor to the globalization literature, who also distinguishes three types of explanation: (1) market-based explanations; (2) institutional-technological explanations; and (3) political explanations, which in turn are subdivided into interpretations that, like Sobel's, stress internal political processes, or, like Helleiner's, stress the autonomous state.[8] The organization of inquiry seems to be treated very much as a matter of personal taste.

If historical interpetation is to be of much value to social scientists, however, it should, ideally, be framed to facilitate the closest possible comparison with prevailing theoretical perspectives and approaches—in effect, to offer a form of empirical test of alternative analytical models. In the IPE field today three broad paradigms dominate most discussion, the familiar three levels of analysis: the systemic (or structural) level of analysis, the domestic (or unit) level, and the cognitive.[9] Specific theories tend to represent a variation on one or more of these general themes. It would seem preferable, therefore, as a general principle, to organize inquiry into the sources of financial globalization along the same lines.

This suggests a taxonomy of four main hypotheses for investigation. At the systemic level, two variants can be identified, replicating Helleiner's distinction between the contrasting roles of market forces and government policies. One variant, with roots in standard neoclassical economics, stresses the powerful impacts of competition and innovation in the financial marketplace. It also emphasizes advances in communications and information technologies, which have literally swept away institutional and legal barriers to market integration and the free flow of capital. This variant might be labeled the "liberal model." The second, more consistent with an older tradition in international relations theory, emphasizes the determining role of policy rivalry among governments in an insecure world, each calculating how best to use its influence and capabilities to promote state interest. Call

[8] Philip G. Cerny, "The Deregulation and Re-regulation of Financial Markets in a More Open World," in Cerny (fn. 3), chap. 3.

[9] Each of these levels of analysis has its analogue in one of Kenneth Waltz's three "images" of international relations—respectively, the third, second, and first image. See Waltz, *Man, the State and War* (New York: Columbia University Press, 1959).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

this the "realist model." A third approach, pitched at the unit level of analysis characteristic of most comparative political economy, corresponds to Sobel's inside-out explanation, highlighting the role of domestic politics and institutions in driving international developments. This may be labeled the "pluralist model." A fourth approach, embodying Helleiner's ideational factors, underscores the role of belief systems and epistemic communities as catalysts for change. Call this the "cognitive model."

The question is: What does the historical evidence suggest about the relative utility of each of these four models? Which comes closest to actually explaining the resurrection of global finance? And what are the linkages among them?

Each model has its champions. The liberal model, not surprisingly, is the personal favorite of most economists. Typical is Ralph Bryant, a well-known international monetary specialist, who confidently asserts that "technological nonpolicy factors were so powerful . . . that they would have caused a progressive internationalization of financial activity even without changes in government separation fences."[10] On the political science side, the case has been put equally firmly by David Andrews, who emphasizes both the degree to which capital mobility appears to have increased independently of changes in national regulatory frameworks and the degree to which liberalization at the national level has seemingly occurred in response to market pressures at the systemic level.[11] Appearances, however, can be deceiving. An approach that causally links an outcome (globalization) to its own defining characteristics (competition and innovation) borders on the tautological. It also leaves no room for politics in an arena, the interstate system, that is inherently politicized.

A possible antidote is offered by the realist model, which is nothing if not political. Reversing the arrow of causation, the approach is best represented by Helleiner. "The contemporary open global financial order," he argues, "could never have emerged without the support and blessing of states" (p. vii). Capital mobility may have been facilitated by innovations in financial instruments and advances in communications and information technologies. Without explicit policy decisions by governments, however, national markets would have remained as insulated from one another as ever. Political authorities promoted the res-

[10] Ralph C. Bryant, *International Financial Intermediation* (Washington, D.C.: Brookings Institution, 1987), 69.

[11] Andrews (fn. 3). See also Philip G. Cerny, "The Dynamics of Financial Globalization: Technology, Market Structure, and Policy Response," *Policy Sciences* 27, no. 4 (1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

urrection of global finance by granting more freedom to market operators, refraining from imposing more effective controls on capital movements, and acting to prevent or manage international financial crises.

Three issues, however, are raised by the realist model. First, if states were so pivotal in the globalization process, could they also turn back the clock if they wish? Reversibility would appear to be a logical corollary of the realist model. Certainly this is the conclusion drawn by Helleiner, who in more recent commentary has argued quite forcefully that since "financial globalization [was] heavily dependent on state support and encouragement . . . a reversal of the liberalization trend is more likely than is often assumed."[12] Others, however, attack the implication, insisting instead on a kind of hysteresis in financial market development. Globalization has progressed so far, it is said, that capital mobility must now be regarded as tantamount to an exogenous feature of the international system. In the words of David Andrews, "The constraints imposed on states by capital mobility are structural in nature, or at a minimum can usefully be construed as structural by analysts."[13]

In fact, both sides of this debate seem too categorical. Central to the issue is an implicit calculation of the costs, economic or political, that would be associated with any attempt to restrict capital mobility. Reversibility would not appear to be ruled out in principle. In practice, however, limits seem likely only insofar as governments are prepared to pay the requisite price. As Louis Pauly has contended,

> Capital mobility constrains states, but not in an absolute sense. . . . Analysts should therefore be cautious when interpreting the current dimensions of international capital flows as constituting an exogenous structure that irrevocably binds societies or their states. . . . A collective movement away from capital decontrol may be undesirable, but it remains entirely possible.[14]

We will return to this crucial point below.

A second issue has to do with matters of power and hegemony in the globalization process. Helleiner and Sobel alike stress the role that American and British leadership played in opening up financial mar-

[12] Eric Helleiner, "Post-Globalization: Is the Financial Liberalization Trend Irreversible?" in Daniel Drache and R. Boyer, eds., *The Future of Nations and the Limits of Markets* (forthcoming).

[13] Andrews (fn. 3), 197. See also idem, "Capital Mobility and Monetary Adjustment in Western Europe, 1973–1991," *Policy Sciences* 27, no. 4 (1994); Philip G. Cerny, "The Political Economy of International Finance," in Cerny (fn. 3), chap. 1; and idem (fn. 11).

[14] Louis W. Pauly, "Capital Mobility, State Autonomy and Political Legitimacy," *Journal of International Affairs* 48 (Winter 1995), 373, 385. Andrews himself (fn. 3) admits that "this is not to say that the current degree of capital mobility cannot be reduced, but instead that reduction is likely to be both difficult and costly" (p. 198).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

kets. To borrow from the language of Scott James and David Lake,[15] however, we may ask which "face" of hegemony was at work here: the first face of direct government-to-government influence, exercised through positive and negative sanctions; the second face of market power, altering incentive structures; or the third face of ideas and ideology, shaping the climate of opinion. Except in the special case of Japan, neither Helleiner nor Sobel suggests much evidence of overt inducements or threats by Washington or London to compel liberalization by other governments.[16] Indeed, as indicated, Sobel explicitly rejects any explanation positing direct exercise of state influence. They differ sharply, however, about which of the other two faces mattered more in this context.

For Helleiner, it was the second face—initially, the pressures created by U.S. and U.K. policy decisions facilitating creation of a foreign-currency deposit market, the Euromarket, in London. "When these two states supported growth of the Euromarket . . . foreign financial centers . . . were forced to follow the lead of Britain and the United States by liberalizing and deregulating their own financial systems" (p. 12). For Sobel, by contrast, it was the third face, exhibited in particular by the United States—the privileging of American-style rules, institutions, and trading technologies in foreign securities markets:

> Through innovation and invention of financial and regulatory technologies, U.S. actors established the agenda and boundaries of changes in other markets. . . . This embedded influence produces an outcome generally consistent with U.S. actors' preferences, as others choose options already enacted in the U.S. market, reducing transaction costs for American firms and professionals overseas, and at far less cost than direct pressure. (pp. 151–52)

In fact, there is nothing inherently contradictory about these two views; they are complementary rather than mutually exclusive. They do suggest, however, different inferences about the comparative importance of government policies versus market forces, and thus ultimately about the explanatory power of the realist versus the liberal model. More detailed empirical studies to help disentangle the two forms of influence would clearly be useful.

[15] Scott C. James and David A. Lake, "The Second Face of Hegemony: Britain's Repeal of the Corn Laws and the American Walker Tariff of 1846," *International Organization* 43 (Winter 1989).

[16] Uniquely, Japan was the object of considerable and quite direct pressure from the United States to liberalize its financial markets, particularly during the 1980s. For detail, see Rosenbluth (fn. 7), chap. 3. Overt exercise of influence by the U.S. as well as Britain has been much more evident in the negotiation of regulatory responses to financial globalization, as Kapstein emphasizes (chap. 5).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

A third issue, finally, has to do with the motivations for state behavior suggested by the realist model. Were states operating as classic rational unitary actors, single-mindedly competing within systemic constraints to maximize some objective measure of national interest? Or were other, more subtle forces at work to shape government preferences and perceptions? This, of course, is the issue posed by the pluralist and cognitive models, both of which effectively open up the black box of public policy.

Sobel's inside-out explanation offers a prime example of a pluralist model. His view that "internationalization [was] motivated domestically" (p. 155) is echoed by such scholars as Ron Martin, who asserts that globalization was in fact "politically engineered . . . a reassertion by the state of an underlying disposition towards financial interests."[17] Similarly, Helleiner's references to ideological shifts and epistemic communities exemplify well the main elements of the cognitive model, also echoed by others. The former element, the role of ideas, is highlighted as well by Cerny, who stresses "an ideological backlash against state economic interventionism" as a key part of the dynamic driving market deregulation.[18] The latter element is highlighted as well by Stephen Gill and David Law, who in quasi-Marxist language stress

> international patterns of elite interaction . . . [which] are explicitly concerned to foster . . . a shared outlook among the international establishments of the major capitalist countries . . . [and] to produce a transnational capitalist class or class fraction with its own particular form of "strategic" class consciousness.[19]

Plainly, the array of potential influences behind state policy is both diverse and complex.

So how did globalization happen? Amidst the cacophony of voices championing one or another version of events, the relative utility of the four models and the interrelationships among them remain unclear. Most sources, wary of monocausal interpretations of history, appear to concur with Cerny's assertion that "it is impossible to rely on any one form of explanation."[20] Many seem tempted to fudge the issue simply by citing multiple factors more or less indiscriminately. With their care-

[17] Ron Martin, "Stateless Monies, Global Financial Integration and National Economic Autonomy: The End of Geography?" in Corbridge, Thrift, and Martin (fn. 3), 271.

[18] Cerny (fn. 8), 51. Andrews (fn. 3), similarly speaks of the critical role of "widely shared ideological commitments" and "mindsets" (pp. 200–201).

[19] Gill and Law (fn. 3), 483–84.

[20] Cerny (fn. 8), 79.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

fully executed historical studies, Helleiner and Sobel stand as worthy exceptions to more general practice. Yet even their treatments fall rather short of the demands of complete and formal comparative analysis. Helleiner, while stressing the role of government policies, may certainly be faulted for failing to go behind observed decisions to explore fully alternative motivations for state behavior. Sobel, meanwhile, intent on proving his inside-out hypothesis, appears to understate greatly the role that external forces undoubtedly played in eroding internal resistance to change. Sobel also appears to contradict himself by insisting on the significance of residual distinctions between national markets even while simultaneously alleging homogenization of financial technologies through the embedded influence of U.S. actor preferences. Given such gaps and inconsistencies, it is evident that we are still far from resolving the central question of causation.

A fuller explanation would focus on dynamic linkages among factors highlighted by the four models, particularly as they influenced state calculations of interests over time. A hint of what this might look like is suggested by John Goodman and Louis Pauly, who note a powerful dialectic at work in the relationship between market forces and public policy—government actions in one period leading to increases of capital mobility that in turn have generated pressures for widening liberalization in subsequent periods.[21] A prime example was the Interest Equalization Tax imposed by the United States in 1963 in an effort to stem foreign-bond sales in New York. One consequence was the stimulus this provided to growth of the Eurocurrency market in London, which in turn eroded the effectiveness and raised the cost of existing restrictions on financial flows and eventually led governments to grant even more freedom for private operations. "In this sense," Goodman and Pauly write, "the diminishing utility of capital controls can be considered the unintended consequence of other and earlier policy decisions."[22] What we need now is more rigorously detailed study along such lines, not just to compare alternative hypotheses but, more importantly, to explore the complex underlying connections among them.

[21] Goodman and Pauly (fn. 3), 79. Andrews (fn. 3) criticizes Goodman and Pauly for this suggestion, charging that, by stressing both market forces and preexisting levels of financial integration, they in effect "treat capital mobility as both an independent and dependent variable" (p. 197). In fact, this is a bit unfair, since Goodman and Pauly clearly have in mind a kind of dynamic sequencing model or step-function in which today's dependent variable is tomorrow's independent variable (and vice versa).

[22] Goodman and Pauly (fn. 3), 79.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## What Does It Mean?

Even less consensus exists concerning the consequences of financial globalization. As the divergent results of the remaining books make clear, views range from the hopeful to the hopeless. Some economists, with their faith in neoclassical theory, might argue optimistically that the resurrection of global finance represents, in effect, the best of all possible worlds. Other observers, more pessimistically, might simply nod their heads sadly in agreement. At issue is the role of markets versus governments in the management of international capital. Are we better off if the phoenix rules the roost? Or do we simply have no choice?

Analytically, the consequences of globalization may be addressed at two very different levels—at the macro level, with implications for aggregate economic performance and the effectiveness of national stabilization policies; and at the micro level, with implications for domestic distribution and the role of public policy in structuring private activity. Sensationalist sources tend cavalierly to compound the two. "Governments at all levels . . . have lost the vestiges of unchecked economic sovereignty," says one;[23] "politicians these days have no doubt where the power lies," asserts another.[24] The distinction between the two levels, however, is critical to a full understanding of practical consequences.

### The Macro Level

The core issue at the macro level, long familiar to economists, is best summarized in terms of what I have elsewhere labeled the "unholy trinity"—the intrinsic incompatibility of exchange-rate stability, capital mobility, and national policy autonomy:[25]

> The problem . . . simply stated, is that in an environment of formally or informally pegged rates and effective integration of financial markets, any attempt to pursue independent monetary objectives is almost certain, sooner or later, to result in significant balance-of-payments disequilibrium, and hence provoke potentially destabilizing flows of speculative capital. To preserve exchange-rate stability, governments will then be compelled to limit either the movement of

[23] McKenzie and Lee (fn. 1), xi.

[24] Millman (fn. 1), 24.

[25] Benjamin J. Cohen, "The Triad and the Unholy Trinity: Lessons for the Pacific Region," in Richard Higgott, Richard Leaver, and John Ravenhill, eds., *Pacific Economic Relations in the 1990s: Cooperation or Conflict?* (Boulder, Colo.: Lynne Reinner, 1993). Adding free trade to the equation produces what Tommaso Padoa-Schioppa calls the "inconsistent quartet." See Padoa-Schioppa, "The European Monetary System: A Long-term View," in Francesco Giavazzi, Stefano Micossi, and Marcus Miller, eds., *The European Monetary System* (Cambridge: Cambridge University Press, 1988).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

> capital (via restrictions or taxes) or their own policy autonomy (via some form of multilateral surveillance or joint decisionmaking). If they are unwilling or unable to sacrifice either one, then the objective of exchange-rate stability itself may eventually have to be compromised. Over time, except by chance, the three goals cannot be attained simultaneously.[26]

As capital mobility has increased, so too has concern about its implications for the effectiveness of independent monetary and fiscal policies.[27] Goodman's study, though focused on central banking alone, is typical. With accelerating financial globalization, he suggests, a government's room for maneuver is necessarily reduced. In effect, the stringent logic of the unholy trinity imposes an increasingly stark trade-off on policymakers. Autonomy of national policy can be preserved only by giving up some degree of currency stability; an independent exchange-rate target can be maintained only at the cost of reduced control over domestic macroeconomic performance. Over time, states begin to pay a higher price for divergent behavior owing to the risk of capital flight. Ultimately, the cost of defending policy independence may simply become too high to bear. In Goodman's view, these developments have therefore "increased the overall pressure for monetary convergence [and] created new incentives for monetary policy cooperation" (p. 217). Andrews, concurring, calls this the "capital mobility hypothesis":[28] "The central claim associated with the capital mobility hypothesis is that integration has increased the costs of pursuing divergent monetary objectives, resulting in structural incentives for monetary adjustment."[29]

How serious is the challenge of the capital mobility hypothesis? Certainly examples abound that would seem to testify to the strength of the constraint imposed on governments. Goodman cites the case of France in 1983, where at a time of sluggish growth in Europe a new socialist administration was compelled to abandon its agenda of unilateral expansion by a speculative run on the franc (pp. 126–39). More recently, beginning in late 1994, much the same happened to Mexico when foreign as well as domestic investors lost confidence in the country's economic management, forcing incoming President Ernesto Zedillo to introduce an austerity program of unprecedented severity. Once Mexico's bond rating was marked down by agencies like Moody's Investors

[26] Cohen (fn. 25), 147.

[27] See esp. Michael C. Webb, "International Economic Structures, Government Interests, and International Coordination of Macroeconomic Adjustment Policies," *International Organization* 45 (Summer 1991); Goodman and Pauly (fn. 3); Cohen (fn. 25); Andrews (fn. 3).

[28] Andrews (fn. 3).

[29] Ibid., 203.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Services, the handwriting was on the wall. Policymakers had to do whatever they could to restore their own credibility. As one commentator observed:

> That makes Moody's one powerful agency. In fact, you could almost say that we live again in a two-superpower world. There is the U.S. and there is Moody's. The U.S. can destroy a country by leveling it with bombs; Moody's can destroy a country by downgrading its bonds.[30]

In reality, however, the discipline of the financial marketplace may be less than it appears for at least three reasons. In the first place, there are limits to just how much can be accomplished by independent monetary and fiscal policies even in the absence of a high degree of capital mobility. The challenge to policy autonomy matters only to the extent that available policy instruments (the money supply or government budget) can be assumed to have a genuine influence on "real" economic variables like output and employment. In effect, there must be some sustained trade-off between unemployment and inflation—technically, a negative slope to the Phillips curve. Today, however, the conventional view among economists, inspired by so-called rational-expectations theory, is that there is no such trade-off, at least not for long—no permanent slope to the Phillips curve. Over relatively extended time horizons, policy is more apt to be neutral with respect to real output, influencing only prices or interest rates. Monetary or fiscal initiatives may have a significant impact on aggregate performance, but their effects are not likely to be lasting. Insofar as policy autonomy continues to matter, therefore, it is mostly for the short term.

Second, it is also important to recall the still limited scope of financial globalization in the contemporary world. The power of Moody's to destroy a country is effectively contained to the extent that capital mobility remains short of absolutely perfect. As Sylvia Maxfield has pointed out, moreover, not all international investors are equally sensitive to monetary or fiscal changes in host countries.[31] Governments thus still retain some room for maneuver to pursue independent policy objectives.

[30] Thomas A. Friedman, "Don't Mess with Moody's," *New York Times*, February 22, 1995, p. A15. For a more general analysis of the role that credit-rating agencies may play in constraining public policy, see Timothy J. Sinclair, "Between State and Market: Hegemony and Institutions of Collective Action under Conditions of International Capital Mobility," *Policy Sciences* 27, no. 4 (1994). For more specific detail on the Mexican experience, see Moises Naim, "Mexico's Larger Story," *Foreign Policy* 99 (Summer 1995).

[31] Sylvia Maxfield, "International Portfolio Flows to Developing/Transitional Economies: Impact on Government Policy Choice" (Manuscript, Yale University, 1995).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Finally, it is important to recall that, within limits, a trade-off continues to exist between policy autonomy and currency stability. Even if a capital flight does develop, officials have some choice—to sacrifice either domestic targets or the exchange rate. Investors anxious to switch out of local assets must, collectively, find buyers for their claims. Unless the central bank steps in as residual buyer of its own currency, however, the impact of a loss of confidence will be seen in asset prices and the exchange rate rather than in the government's own programs. In other words, economic policies at home need not be fatally compromised as long as the authorities are willing and able to tolerate a degree of currency volatility abroad.

In practice, to be sure, this is a luxury that not all economies are able to afford. The insulation provided by a floating exchange rate is partial at best: most countries find it difficult to protect themselves completely from all the negative consequences of currency instability. For economist Barry Eichengreen, this means that the logic of the unholy trinity has now in effect eliminated the policy-autonomy trade-off altogether. Governments, he argues, can no longer hope to contain market pressures by means of contingent exchange-rate rules. In the future, "countries that have traditionally pegged their currencies will be forced to choose between floating exchange rates on the one hand and monetary unification on the other. . . . The middle ground of pegged but adjustable rates and narrow target zones is being hollowed out."[32] But this conclusion rests on an unspoken, and highly debatable, judgment about the political calculations involved. Eichengreen asserts that "the capital mobility characteristic of the late twentieth century" makes pursuit of independent policy objectives "extremely costly and potentially unsustainable politically."[33] Note, however, that it does not make national autonomy impossible. The option continues to exist, albeit at a price. How can we be sure what price will turn out to be unsustainable politically?

Thus while the challenge of the capital mobility hypothesis is obviously serious, and no doubt growing, governments do not appear in fact to have been wholly deprived of macroeconomic authority—at least, not yet. The interesting question, therefore, is not whether financial globalization imposes a constraint on sovereign states; it most clearly does. Rather, we should now be asking how the discipline works and under what conditions. What accounts for the remaining room for maneuver, and why do some countries still enjoy more policy autonomy

[32] Barry Eichengreen, *International Monetary Arrangements for the 21st Century* (Washington, D.C.: Brookings Institution, 1994), 5–6.

[33] Ibid., 60.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

than others? These issues point the way for future research in this area. It is time to move beyond broad generalizations about the logic of the unholy trinity to more disaggregated analysis of the complex linkages between global finance and domestic performance.

On these linkages, only a few intriguing hints can be found in the literature to date. Goodman, for example, stresses the role of central-bank independence in enhancing the credibility of a state's macroeconomic policies. A monetary authority that is legally distinct from the elected government can give greater assurance that decisions will be insulated from domestic political pressures. The argument appears to have something of a catch-22 quality about it, since it suggests that the only way to avoid speculative capital flows is to do what the market wants; in effect, to save policy autonomy, it must be surrendered. There may nonetheless be an important insight here, if reputation today provides some room for maneuver, if needed, tomorrow. The degree of central-bank independence, along with structural differences in relations between private banks and industry, is also stressed by Randall Henning as a crucial determinant of national-policy choices involving the exchange rate.[34] Along somewhat different lines, Goodman and Pauly emphasize "generic types of external pressure,"[35] which are identified with persistent current-account surpluses or deficits in the balance of payments. Since in standard monetary theory such imbalances are understood to reflect an economy's underlying saving and investment propensities, this amounts to suggesting a systematic difference between capital importers and capital exporters in their respective vulnerabilities to market forces. Andrews, meanwhile, mentions size and openness as factors that may help account for variations in state willingness to tolerate trade-offs of currency volatility for policy autonomy.[36]

Plainly, more could be done to explore linkages of these kinds. Particular use might be made of the contemporary theory of optimum currency areas (OCAs), well developed by economists, which highlights the advantages or disadvantages, as seen from a single country's point of view, of abandoning monetary sovereignty to participate in a currency union or an equivalent regime of irrevocably fixed exchange rates.[37] OCA

[34] C. Randall Henning, *Currencies and Politics in the United States, Germany, and Japan* (Washington, D.C.: Institute for International Economics, 1994).

[35] Goodman and Pauly (fn. 3), 51.

[36] Andrews (fn. 3), 206–7.

[37] For recent surveys of OCA theory, see Paul R. Masson and Mark P. Taylor, "Currency Unions: A Survey of the Issues," in Masson and Taylor, eds., *Policy Issues in the Operation of Currency Unions* (New York: Cambridge University Press, 1993); and George S. Tavlas, "The 'New' Theory of Optimum Currency Areas," *World Economy* 16 (November 1993).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

theory identifies a number of key characteristics that may be regarded as instrumental in a government's decision to surrender authority over its exchange rate. In addition to a country's size and openness, these include such economic variables as wage and price flexibility, factor mobility, geographic trade patterns, the degree of commodity diversification, inflation trends, and the source and timing of payments disturbances. These particular characteristics are singled out because they may be assumed to influence, to a greater or lesser extent, the degree of insulation afforded by a floating currency. To this list one might also add political variables such as state capacity, electoral politics, and foreign alliance or treaty commitments. The number of conditions that might influence the preferred trade-off between policy autonomy and exchange-rate stability is quite large. What is needed is more careful applied investigation of how each works in today's financially integrated world.

### The Micro Level

The core issue at the micro level is the familiar one of whose ox is gored: who wins and who loses? As Frieden has reminded us, increased capital mobility may be "expected to have a significant impact on the interests of various domestic economic interest groups."[38] It is also likely to influence government's ability to structure economic activity by remaking political coalitions and changing the pattern of lobbying over national policies.[39] Here too increasing concern is expressed about possible barriers to the attainment of politically determined social goals. In Paulette Kurzer's words:

> The growth of financial activities and the availability of many different kinds of financial instruments are major stumbling blocks for governments that desire to induce an increase in production or investments or a change of prices. . . . High capital mobility and deepening financial integration prompt governments to remove or alter institutions and practices objectionable to business and finance. (pp. 7, 245)

The key, of course, is the financial sector's increased ability simply to take its money elsewhere. Recalling the language of Albert Hirschman, the bargaining strength of different groups in an economy may be thought to depend on the relative availability of the options of exit,

[38] Frieden (fn. 4), 433.
[39] Ibid.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

voice, and loyalty.[40] The greater a group's capacity to evade the preferences of public officials (exit), the more likely it is to give voice within the political system to promote its own desires and objectives. The government's ability to command loyalty will be correspondingly weakened. Financial globalization clearly enhances the leverage of investor interests by reducing barriers to exit. Owners of mobile capital thus gain influence at the expense of less fortunate sectors, including so-called national capital as well as labor. As Gill and Law put it, "The impact of increased capital mobility . . . has worked to the advantage of large-scale transnational capital, relative to national capital . . . and to labor, especially in the core capitalist states. . . . These changes can be interpreted as signs of the emergence of a new regime of accumulation."[41]

The result, many scholars fear, is likely to be both a dramatically more regressive income distribution and an effective veto over public policy. Wages will tend to fall relative to returns on capital, eroding the living standards of many citizens.[42] Even worse, governments will increasingly find themselves hostages to financial-market sentiment, compelled to take account of investor concerns at every turn. More than a decade ago Robert Bates and Da-Hsiang Lien explained how, historically, increases in the mobility of taxable property have always obliged political authorities "to bargain with those who possessed property rights over the moveable tax base and to share with them formal control over the conduct of public affairs."[43] Today, with the resurrection of global finance, that imperative seems stronger than ever. Redistributive strategies are out; tax relief for financial interests is in.

Certainly Kurzer's study would seem to confirm the validity of such fears. In each of the four countries she examines, the abandonment of policies traditionally associated with social democracy—including numerous entitlement programs; redistributive incomes policies; and consensual tripartite exchanges among business, labor, and government—

[40] Albert O. Hirschman, *Exit, Voice and Loyalty: Responses to Decline in Firms, Organizations, and States* (Cambridge: Harvard University Press, 1970).

[41] Gill and Law (fn. 3), 486–88.

[42] See, e.g., Thomas I. Palley, "Capital Mobility and the Threat to American Prosperity," *Challenge* (November–December 1994).

[43] Robert H. Bates and Da-Hsiang Donald Lien, "A Note on Taxation, Development, and Representative Government," *Politics and Society* 14 (March 1985), 57. Bates and Lien note that their argument leads them to precisely the opposite conclusion from Hirschman, who reasoned that it was owners of immobile resources who would be more likely to take the political initiative. Hirschman's error, they suggest, was to focus on the motivations of private groups alone without regard to their strategic interaction with government. Political authorities anxious to preserve their tax base will always pay more attention to the owners of mobile resources. Ibid., 61.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

clearly appears linked to the postwar internationalization of finance. "This mobility allows business and finance to move with ease across borders into different money-making ventures and away from arrangements considered inflexible and outdated" (pp. 4–5). Ultimately, in all four countries, officials concluded that the cost of policy independence had become more or less unacceptable. None wished to provoke a major capital flight. Jonathan Moses offers a similar interpretation of the parallel experiences of Sweden and Norway:

> Despite the fact that Sweden and Norway can be said to have relied on different strategies for meeting social democratic objectives, both strategies have proved ineffective in the new international economic environment. . . . A new international economic regime, characterized by increased levels of capital mobility, has made traditional tools for government steering ineffective. . . . [A]ll participants are subject to an iron law of policy.[44]

Broad evidence suggesting such an iron law can also be found in the recent evolution of national tax regimes, not only in Europe but in many other countries as well, including the United States. During the 1980s, which has been described as the "decade of tax reform," governments on every continent initiated major revisions in their tax codes designed inter alia to reduce marginal tax rates on capital and to restrict the use of tax policy as an instrument of economic management. Most specialists agree that a principal cause of these moves has been the fear of investor exodus made easier by the growing integration of financial markets. In the words of Sven Steinmo, "The battle for progressive (if not redistributive) taxation has been a difficult one. . . . But as the power resources available to capital increase with its growing internationalism, it may be that the difficult battle will become a futile one."[45]

In practice, however, here too the discipline of the marketplace may be less than it appears. The indictment of global finance seems extreme. First, factors other than capital mobility may also have contributed to the outcomes described by Kurzer and others. To single out financial internationalization alone may be to mistake correlation for causation.[46] Even with greater options for exit, moreover, capital's veto is not ab-

[44] Jonathan W. Moses, "Abdication from National Policy Autonomy: What's Left to Leave?" *Politics and Society* 22 (June 1994), 140–42.

[45] Sven Steinmo, "The End of Redistribution? International Pressures and Domestic Tax Policy Choices," *Challenge* (November–December 1994), 17.

[46] Thus Ton Notermans criticizes Jonathan Moses for his preoccupation with capital mobility in explaining the Swedish and Norwegian experiences, to the exclusion of what Notermans regards as even more important domestic factors. Notermans, "Social Democracy in Open Economies: A Reply to Jonathan Moses," *Politics and Society* 22 (June 1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

solute. The globalization of finance obviously has increased pressures for general policy convergence toward an agenda set by investors. But a closer look suggests that room may still exist for implementation or preservation of distinctive national strategies and structures. Geoffrey Garrett and Peter Lange, for example, stress the role of more selective supply-side programs, such as policies targeted to shape investment incentives or labor-market practices, which have enabled "governments of the left" to maintain traditional redistributive and welfare goals while simultaneously adjusting to the demands of investor interests.[47] Financial-market integration has not made separate social goals impossible, they argue. Rather, it "has altered the policy instruments through which governments can pursue their partisan objectives."[48] Likewise, Pauly has emphasized the extent to which diversity in national financial structures persists despite increasing international mobility of capital.[49] The iron law would appear to be less of a handicap than commonly thought.

Hence once again the interesting question is not whether financial globalization imposes a constraint, but how and under what conditions. Here too it is time to move beyond broad generalizations to a more disaggregated analysis of the diverse relationships at work. One key might lie in the distinction between national and transnational capital, which could help to explain observed differences in pressures for convergence at the sectoral level. As Frieden has noted, "Inasmuch as capital is specific to location, increased financial integration has only limited effects on policies targeted at particular industries."[50] Other keys might be located in domestic institutional variations of the sort examined by Kurzer or in differential interest-group pressures as emphasized by Helen Milner.[51] These could be thought to affect the ability or willingness of political authorities to bear the costs of policy independence. At the micro level no less than at the macro level, more careful applied investigation is needed to see how any of these linkages might actually work.

[47] Geoffrey Garrett and Peter Lange, "Political Responses to Interdependence: What's 'Left' for the Left?" *International Organization* 45 (Autumn 1991).

[48] Ibid., 541.

[49] Louis W. Pauly, "National Financial Structures, Capital Mobility, and International Economic Rules: The Normative Consequences of East Asian, European, and American Distinctiveness," *Policy Sciences* 27, no. 4 (1994).

[50] Frieden (fn. 4), 430.

[51] Helen V. Milner, "Bargaining and Cooperation: Domestic Games and International Relations" (Manuscript, Columbia University, 1995).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## What Can Governments Do about It?

The practical consequences of financial globalization thus seem rather more nuanced and contingent than they appear at first glance. Increases of capital mobility have clearly diminished the effective autonomy of states. On the other hand, public officials still retain some room to pursue independent policy agendas. Across countries as well as over time, outcomes may vary considerably depending on an identifiable range of economic and political factors. From a political-economy perspective, therefore, it would seem important to ask what governments can do, if anything, to promote outcomes more to their liking. Even if it does not rule the roost, the phoenix can make life difficult for policymakers. Can it be tamed?

This brings us back to the issue of reversibility. To relax the constraint on policy, capital mobility would have to be reduced significantly, or at least managed more successfully. This would no doubt be both difficult and costly. Are governments prepared to pay the price? Two broad strategies seem possible, one unilateral and one collective. Neither is without problems.

The first approach would be the more direct. States would simply seek to limit capital mobility on an individual basis. In principle, any government has the means available to reverse the process of financial integration for its own economy. All it requires is the will to impose new taxes or controls of sufficient severity to effectively eliminate opportunities for substitution between domestic and foreign claims. As Pauly suggests, "states can still defy markets" if they so desire.[52] The costs involved, both economic and administrative, are apt to be quite high, however, unless all governments are prepared to act in concert. In practice, therefore, comprehensive unilateral initiatives would seem unlikely except in the most dire of circumstances, such as a foreign-exchange or national-security crisis.

The alternative, collective approach would seek to promote policies of active collaboration to ease or eliminate the constraints imposed by financial integration. This is the path advocated by both Goodman and Kapstein. While disagreeing on specifics, both scholars concur on a general need for political governance to catch up with global finance. In Kapstein's words, "The idea of globalization challenges public officials, who are responsible to their societies for ensuring economic wel-

[52] Pauly (fn. 14), 373.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

fare and national security. In an international system which lacks any higher authority, citizens must look to the state for the protection of their well-being" (p. 1). Governments thus must be prepared to merge selected elements of their sovereignty to preserve their capacity to fulfill established responsibilities.

Is cooperation feasible? Skepticism would appear justified by recent history. During the 1980s, the so-called Group of Seven industrial states (the United States, Britain, Canada, France, Germany, Italy, and Japan) repeatedly declared their commitment to principles of mutual surveillance of their macroeconomic policies and a coordinated management of exchange rates. Yet for all their promises to curb unilateralist impulses, the governments involved more often than not ended up going their separate ways as policymakers wearied of the frequent concessions required. Collaboration in practice tended to ebb and flow like the tides. Apparently, as I have written before, international monetary cooperation, like passionate love, is a good thing but difficult to sustain.[53] The episodic quality of such efforts has also been demonstrated by more recent events in Europe. The march toward a European monetary union, which Goodman approvingly discusses in considerable detail, has seemingly been stalled by currency crises occurring since the completion of his study. Goodman's barely qualified positive tone plainly reflects the enthusiasm and sense of momentum generated by passage of the Maastricht treaty in 1991, when he was writing. Today, it seems fair to say, prospects for a single European currency and central bank appear rather dim.

Reasons for the problematic quality of cooperation are not difficult to find. At the domestic level, as indicated, financial globalization remakes political coalitions and creates vested interests in the new status quo. In the words of Goodman and Pauly, "Global financial structures affect the dynamics of national policy-making by changing and privileging the interests and actions of certain types of firms. Once those interests have been embedded in policy, movement back is not necessarily precluded but is certainly rendered much more difficult."[54] At the systemic level, states are always tempted to vie for advantage at the expense of rivals. To the extent that governments act as "defensive positionalists,"[55] compromise will be inhibited by fears of noncompli-

[53] Cohen (fn. 25), 134.
[54] Goodman and Pauly (fn. 3), 52.
[55] Joseph M. Grieco, "Anarchy and the Limits of Cooperation: A Realist Critique of the Newest Liberal Institutionalism," *International Organization* 42 (August 1988).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

ance abroad as well as of relative loss at home. Factors at both levels enhance the attractiveness of policies of unilateralism and even aggressive neomercantilism in financial matters. For some observers, they virtually guarantee a world dominated by the "competition state."[56]

Yet again, some caution is warranted in the face of such bold generalizations. If the extensive literature on international regimes teaches us anything, it is that even the most self-interested of states will on occasion find it advantageous to voluntarily limit their own autonomy.[57] This will especially be so when governments are confronted with what Arthur Stein calls "dilemmas of common aversions" rather than "dilemmas of common interests."[58] Dilemmas of common aversions, or coordination games, exist when all actors share a concern to avoid a particular outcome. The only question is how to establish a norm, or focal point, around which behavior may coalesce. Beyond agreeing to play by some standard set of rules (for example, driving on the right-hand side of the road), no compromise of underlying preferences is called for. This is in contrast to dilemmas of common interests, or conflictual games, where reciprocal concessions are indeed required to avoid suboptimal (Pareto-deficient) outcomes. Collective action in such situations will obviously be more difficult to achieve or sustain. The difference between the two classes of dilemma is reflected in the distinction economist Peter Kenen draws between two types of cooperation —the "policy-optimizing" approach, where governments seek to bargain their way from suboptimality to something closer to a Pareto optimum; and the regime-preserving, or public-goods approach, where mutual adjustments are made for the sake of defending existing arrangements or institutions against the threat of economic or political shocks.[59] The more difficult of the two is clearly the policy-optimizing approach. Happily, though, not all of the challenges posed by global finance are quite so demanding.

In fact, many of the issues involved clearly are more in the nature of coordination games, where "regime preservation" rather than "policy optimization" is at stake. One example is the problem studied by

[56] Cerny (fn. 8); and idem, "The Infrastructure of the Infrastructure? Toward 'Embedded Financial Orthodoxy' in the International Political Economy," in Ronen P. Palen and Barry Gills, eds., *Transcending the State-Global Divide: A Neostructuralist Agenda in International Relations* (Boulder, Colo.: Lynne Rienner, 1994).

[57] For a useful recent survey, see Volker Rittberger, ed., *Regime Theory and International Relations* (New York: Oxford University Press, 1993).

[58] Arthur A. Stein, *Why Nations Cooperate: Circumstance and Choice in International Relations* (Ithaca, N.Y.: Cornell University Press, 1990), chap. 2.

[59] Peter B. Kenen, *Managing Exchange Rates* (New York: Council on Foreign Relations, 1988), 75–77.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

Kapstein, international banking regulation. Prudential supervision, Kapstein suggests, presented a "challenging case" because it

> is an issue-area in which state power appears to be relatively weak and ineffective. . . . If, despite these unpromising background conditions, states have somehow managed to build a reasonably sound structure for the regulation and supervision of [banks], maybe this tells us something of more general importance. (p. 178)

In reality, the case may have been less challenging than alleged.[60] All states, after all, share an interest in ensuring prudent behavior in the banking sector, owing to the industry's central role in the operation of the payments system. None was eager to become enmeshed in a competition in laxity. As Kapstein's own analysis demonstrates, few truly serious compromises were actually required to reach agreement on common standards for capital adequacy, accounting rules, and the like. Nonetheless, the case does tell us something of more general importance—that cooperative action is indeed feasible, at least in circumstances where states find themselves confronted with common aversions rather than fundamentally divergent interests.

Such circumstances can be found at both the micro and macro levels. In Sobel's analysis of securities markets, the evidence clearly points to opportunities for regulatory agreements parallel to those highlighted by Kapstein in the banking sector. "The greater the frequency of international trading, the greater the demands for national regulators to coordinate internationally. The more such regulators coordinate, the more regulatory styles will converge" (p. 159).[61] Likewise, even in the G-7's disappointing record of performance in the exchange-rate area, experience testifies to the willingness of governments to act together effectively when broader collective goals have appeared at risk (for example, the Plaza Agreement of 1985, the joint response to the stock-market crash of 1987). While genuine policy-optimizing cooperation in the monetary area remains rare, regime-preserving collaboration has not proved impossible.[62]

Hence, here too the interesting question is not whether but how and

[60] Herring and Litan (fn. 5), chap. 5.

[61] For evidence of developing cooperation in the regulation of securities markets, see Tony Porter, *States, Markets and Regimes in Global Finance* (New York: St. Martin's Press, 1993); and William D. Coleman and Tony Porter, "Regulating International Banking and Securities: Emerging Co-operation among National Authorities," in Richard Stubbs and Geoffrey R. D. Underhill, eds., *Political Economy and the Changing Global Order* (New York: St. Martin's Press, 1994). For some observers, regulatory convergence amounts to a "re-regulation" of financial markets. See Underhill (fn. 3), Cerny (fn. 8).

[62] Cohen (fn. 25); Kenen (fn. 59).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

under what conditions. The difficulties of coordinating state action, whether at the micro or macro level, should certainly not be underestimated. Neither, however, should the problematic quality of cooperative strategies be exaggerated. Some issues by their nature require little more than agreement on mutual recognition of standards. Even in areas where conflicts of interest are more directly involved, it may be possible to preserve or promote a collective approach by switching the focus of attention from one class of policy instruments to another.[63] Short of a genuine systemic crisis, governments may never be willing to pay the undoubtedly steep price that would be required to tame the phoenix completely. But it does appear feasible to arrange life so that states and markets may cohabit a bit more comfortably.

## The End of Geography?

There is no question that the globalization of finance is one of the most striking political-economy developments of the post–World War II era. Governments have clearly been thrown on the defensive. For many analysts, the rise of the phoenix means a possibly irreversible erosion of state authority. For some, it signifies much more: a fundamental change in the meaning of the state itself in relation to transcendent market forces—in effect, a transformation of geography as we know it. No longer is economic activity bounded by the political jurisdiction of the traditional territorial state. Increasingly, the globe itself is the only domain that matters. As economist Richard O'Brien puts it, "The closer we get to a global, integral whole, the closer we get to the end of geography."[64]

Is this the end of geography? At least three intepretations can be attached to O'Brien's proposition. In one sense it could be construed in material terms, to mean a decline in the importance of place—physical location—as markets are increasingly integrated by the forces of competition and technical innovation. New communications and information technologies already permit market actors to operate with impunity across national frontiers. A future could be imagined where financial services are provided and transactions conducted solely in cyberspace, regardless of specific location. This is evidently the meaning that O'Brien mainly has in mind: "As markets . . . become integrated

[63] Webb (fn. 27).

[64] Richard O'Brien, *Global Financial Integration: The End of Geography* (New York: Council on Foreign Relations, 1992), 5. See also Kenichi Ohmae, *The Borderless World: Power and Strategy in an Interdependent Economy* (New York: Harper Business, 1990); Martin (fn. 17).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

. . . the need to base decisions on geography will alter and often diminish."[65] In effect, business will be done anywhere.

Such a scenario, however, tends to strain credulity. In reality, the importance of place is unlikely to be erased completely as long as economies of agglomeration can still be gained from concentrating operations in close proximity. Benefits include the more efficient use of information where contact between market actors is facilitated, the spreading of costs of needed public services, and the ready availability of specialist skills and supporting cognate functions. Even O'Brien admits that "certain activities will still be transacted within a relatively limited physical area, in which a collection of expertise is valuable. . . . Where deals require the personal touch . . . location of the players will still matter."[66] It is no accident that financial markets historically have always tended to gather together in a few select locales; nor that financial centers, once established, generally resist encroachment from newer rivals for long periods of time. As Paul Krugman has reminded us, "increasing returns and cumulative process are pervasive" in influencing the placement of economic activity.[67] Rational actors will continue to be attracted to certain locations as long as gains exceed the costs of congestion.

In a second sense the end of geography could be understood in political terms, as referring to the decline of state authority brought on by financial globalization—the transfer of effective sovereignty from national governments to "stateless" markets. The more public policy is hemmed in by private activities, the less relevant are the legal boundaries that have traditionally been drawn between political jurisdictions. Ultimately, all power might be drained off in favor of transnational capital. The nation-state, as Charles Kindleberger once predicted, would be "just about through as an economic unit,"[68] but this interpretation too tends to strain credulity. As the preceding discussion has sought to make clear, the more plausible scenario is rather more mundane—a world of incomplete discipline and constant tension on both sides of the state-market divide. While national sovereignty is undoubtedly being challenged, it is not yet ready to be tossed quietly into the dustbin of history.

Finally, in a third sense, the end of geography might be interpreted in cognitive terms, as a shorthand expression for a required long-term

[65] O'Brien (fn. 64), 2.
[66] Ibid., 76.
[67] Paul Krugman, *Geography and Trade* (Cambridge: MIT Press, 1991), 25.
[68] Charles P. Kindleberger, *American Business Abroad* (New Haven: Yale University Press, 1969), 207.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

shift of intellectual paradigm. Traditionally, in political economy studies of global finance, the central *problematique* has been the uneasy dialectic between states and markets. As in the books reviewed here, scholars typically focus on the challenge posed by mobile capital to the autonomy of national governments. The existence of an international system, based on state sovereignty as the central organizing principle of world politics, is taken more or less for granted, with markets assumed to operate within a framework defined in terms of the familiar territorial state. As financial activities become increasingly integrated, however, arguably a new organizing principle could be needed, a competing transnational model,[69] based not on political space but on economic space, which is becoming truly global in character. For a widening circle of scholars today, the key to understanding contemporary finance is indeed globalization. As Cerny has contended: "It is not merely the erosion of state financial power, but also the way that separate national currencies themselves are increasingly inextricably locked into wider financial trends and structures, which has become the central issue."[70] Geography has ended in the sense that the very meaning of borders has allegedly dissolved.

In essence, this final interpretation is just another way of arguing for the exogeneity of global finance—the notion that capital mobility must now be regarded as a truly structural constraint on state behavior. The limitations of that perspective have already been addressed. Insofar as the integration of financial markets remains contingent on government calculations of costs and benefits, the traditional statecentric paradigm continues to be relevant. Nonetheless, for students of IPE the competing transnational model is not easy to ignore. It represents, in fact, but one tributary of a much broader stream of criticism of standard international relations scholarship that has been gathering force in recent years.[71] The focus of debate is the "territorial trap,"[72] the deceptively simple notion that world politics can be best understood in terms of

[69] Marcello De Cecco, "Financial Relations: Between Internationalism and Transnationalism," in Roger Morgan et al., eds., *New Diplomacy in the Post-Cold War World: Essays for Susan Strange* (New York: St. Martin's, 1993).

[70] Philip G. Cerny, "Money and Finance in the International Political Economy: Structural Change and Paradigmatic Muddle," *Review of International Political Economy* 1 (Autumn 1994), 591.

[71] John Gerard Ruggie, "Territoriality and Beyond: Problematizing Modernity in International Relations," *International Organization* 47 (Winter 1993); Stephen D. Krasner, "Westphalia and All That," in Judith D. Goldstein and Robert O. Keohane, eds., *Ideas and Foreign Policy: Beliefs, Institutions, and Political Change* (Ithaca, N.Y.: Cornell University Press, 1993); and Janice E. Thomson, "State Sovereignty in International Relations: Bridging the Gap between Theory and Empirical Research," *International Studies Quarterly* 39 (June 1995).

[72] John A. Agnew, "The Territorial Trap: The Geographical Assumptions of International Relations Theory," *Review of International Political Economy* 1 (Spring 1994).

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

"neatly divided spatial packages."[73] In reality, as Stephen Rosow argues, "the entire territorial imagery of current IPE has been rendered ambiguous. . . . Modern conceptualization fails to illuminate the networks and flows of power, and the paths people attempt to carve out within them, which operate in global economic life."[74] To stay useful, contemporary IR scholarship must take more serious account of alternative and potentially complementary conceptualizations of rule and dominion in the modern world—nonterritorial "spaces-of-flows," in the language of John Ruggie, as well as the more traditional territorial "spaces-of-places."[75] The resurrection of global finance can be fully comprehended only in this much broader context.

[73] John A. Agnew, "Timeless Space and State-Centrism: The Geographical Assumptions of International Relations Theory," in Stephen J. Rosow, Naeem Inayatullah, and Mark Rupert, eds., *The Global Economy as Political Space* (Boulder, Colo.: Lynne Reinner, 1994), 89.

[74] Stephen J. Rosow, "On the Political Theory of Political Economy: Conceptual Ambiguity and the Global Economy," *Review of International Political Economy* 1 (Autumn 1994), 473–75.

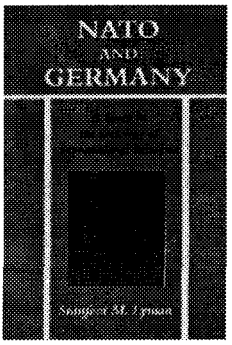
[75] Ruggie (fn. 71), 172.

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# NATO and Germany

*A Study in the Sociology of Supranational Relations*

Stanford M. Lyman




Focusing on the Cold War years, this monograph examines the problems and processes through which the Federal Republic of Germany was formed and admitted into the North Atlantic Treaty Organization (NATO). Considering the current conflict in the Balkans as it relates to the new Germany and the role of NATO, Lyman concludes with suggestions for a basic supranational sociology.

$36.00 cloth (s), 1-55728-389-3

**1-800-626-0090**

**ARKANSAS**
THE UNIVERSITY OF ARKANSAS PRESS
McIlroy House ♦ 201 Ozark Avenue ♦ Fayetteville, AR 72701



STATEMENT OF OWNERSHIP,
MANAGEMENT, AND CIRCULATION, 10/1/95

Title: *World Politics*. Pub. No. 0043-8871. Frequency: Quarterly. Four issues published annually. Subscription price: $56.00 institutions, $25.00 individuals. Location of office of publication: The Johns Hopkins University Press, 2715 North Charles Street, Baltimore, MD 21218. Headquarters of publishers: Same. Publisher: The Johns Hopkins University Press, 2715 North Charles Street, Baltimore, MD 21218. Editor: John Waterbury, World Politics, Bendheim Hall, Princeton, NJ 08544. Owner: Princeton University. The purpose, function, and nonprofit status of this organization and the exempt status for Federal income tax purposes have not changed during the preceding 12 months.

| Extent and nature of circulation | | Av. no. copies each issue preceding 12 mos. | Actual no. copies single issue pub. nearest to filing date |
|---|---|---|---|
| A | Total no. copies printed | 4500 | 4500 |
| B. | Paid circulation, mail subscriptions | 3714 | 3871 |
| C. | Total paid circulation | 3714 | 3871 |
| F. | Free distribution | 140 | 142 |
| G. | Total distribution | 3854 | 4013 |
| H. | Copies not distributed | 646 | 487 |
| I. | Total | 4500 | 4500 |

I certify that the statements made by me above are correct and complete. Marie R. Hansen, Associate Director.


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

THE BROWN JOURNAL OF

# WORLD AFFAIRS

## *Introducing the Broader Spectrum*

**Subscribe Now!**

**Call (401) 521-1767 to Receive a Free Trial Issue**

**IN THE SUMMER 1995 ISSUE**

**The Future of US Foreign Policy**

•

**Political and Economic Reform in Latin America**

•

**Russia in Crisis: The Prospects for Reform**

**PAST CONTRIBUTORS**

**Boutros Boutros-Ghali • McGeorge Bundy • Mangosuthu Buthelezi Herman Cohen • Chester Crocker Alexander Haig • Martin Lee Flora Lewis • Chris Patten Dorothy Solinger**

The *Brown Journal of World Affairs* is a bi-annual publication published at Brown University. Please address all requests for information on subscriptions and article submissions to: **Editorial Office, The Brown Journal of World Affairs, Box 1930 - Brown University, Providence, RI 02912. Tel/Fax: (401) 521-1767**


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## CHADWYCK-HEALEY BUSINESS PUBLICATIONS ON CD-ROM

**THE ECONOMIST**
Keep up with international business and politics, finance, science and technology and the arts across hundreds of issues of **The Economist.**

**FT MCCARTHY**
Find company, industry and marketing information developments from over fifty international newspapers and business magazines, compiled into one database.

**Business research tools on CD-ROM provide speed, accuracy and unparalleled search capabilities.**

**INTLEC — THE INDEX TO INTERNATIONAL ECONOMICS, DEVELOPMENT AND FINANCE**
Focus on global economic trends, international trade and development, and monetary policy, with this database created by the staff of the Joint Bank-Fund Library in Washington, DC.

**LEADERSHIP DIRECTORIES ON CD-ROM**
Access over 350,000 top decision makers in business, government, and professional organizations using the electronic version of the renowned "Yellow Books."

**FINANCIAL TIMES**
Learn about changes in the financial, economic and political arena. **Financial Times** is a leading source of accurate and unbiased news for, the analysis of business events and trends.

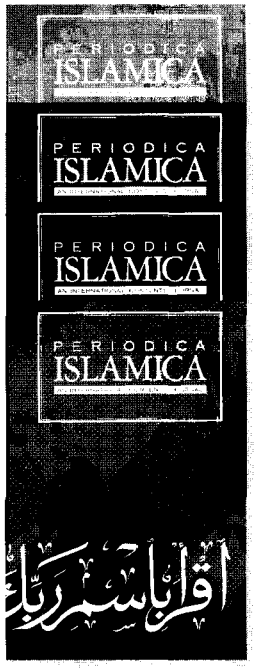
**FOR MORE INFORMATION OR TO ORDER ANY OF THESE INNOVATIVE INFORMATION PRODUCTS, PLEASE CONTACT YOUR CHADWYCK-HEALEY REPRESENTATIVE AT 1-800-752-0515**

CHADWYCK-HEALEY

1101 King Street, Alexandria, VA 22314 (703) 683-4890 Fax: (703) 683-7589
E-Mail: mktg@chadwyck.com Visit our home page at: http://www.chadwyck.co.uk


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# Discover the wide world of Islamic literature




*The journal is produced to a very high standard, and should be a very useful source for all libraries and information users concerned with Islamic issues.*
*Information Development* (London), Volume 7, Number 4, pages 241-242

*This journal is doing a singular service to the cause of the publicity of periodical literature on Islamic culture and civilization in all its diverse aspects. Every scholar of Islamic Studies should feel indebted to you for this service.*
PROFESSOR S.M. RAZAULLAH ANSARI
President, International Union of History and Philosophy of Science (IUHPS)
Commission for Science and Technology in Islamic Civilization, New Delhi, India

*(Periodica Islamica is) an invaluable guide...*
PROFESSOR BILL KATZ
*Library Journal* (New York), Volume 118, Number 21, page 184

Periodica Islamica *is a most valuable addition to our reference collection.*
PROFESSOR WOLFGANG BEHN
Union Catalogue of Islamic Publications, Staatsbibliothek Preussischer Kulturbesitz
Berlin, Germany

*It is recommended for all research libraries and scholars of the Islamic viewpoint.*
DR. RICHARD R. CENTING
*MultiCultural Review* (Westport, Connecticut), Volume 2, Number 1, page 40

*You should be congratulated on* Periodica Islamica *which should prove to be a valuable journal to persons interested in Islam and the entire Muslim World.*
AMBASSADOR (RTD.) CHRISTOPHER VAN HOLLEN
The Middle East Institute, Washington DC, USA

***Periodica Islamica*** is an international contents journal. In its quarterly issues it reproduces tables of contents from a wide variety of serials, periodicals and other recurring publications worldwide. These primary publications are selected for indexing by ***Periodica Islamica*** on the basis of their significance for religious, cultural, socioeconomic and political affairs of the Muslim world.

***Periodica Islamica*** is the premiere source of reference for all multi-disciplinary discourses on the world of Islam. Browsing through an issue of ***Periodica Islamica*** is like visiting your library 100 times over. Four times a year, in a highly compact format, it delivers indispensable information on a broad spectrum of disciplines explicitly or implicitly related to Islamic issues.

If you want to know the Muslim world better, you need to know ***Periodica Islamica*** better.

**Editor-in-Chief ❑ Dr. Munawar A. Anees**
**Consulting Editor ❑ Zafar Abbas Malik**
***Periodica Islamica*, 22 Jalan Liku**
**Kuala Lumpur-59100, Malaysia**

*America Online* • dranees
*CompuServe* • 72260,227
*Delphi* • drmanees
*InterNet* • dranees@klcyber.pc.my

PERIODICA ISLAMICA
AN INTERNATIONAL CONTENTS JOURNAL

## Subscription Order Form

Annual Subscription Rates
❑ Individual US$40.00 ❑ Institution US$249.00

**Name**_____

**Address**_____

**City, State, Code**_____ **Country**_____

❑ Bank draft
❑ coupons
❑ Money order

❑ ❑ ❑ ❑ ❑

❑❑❑❑-❑❑❑❑-❑❑❑❑-❑❑❑❑

Expiration date_____

Signature_____

BY PHONE — To place your order immediately telephone (+60-3) 282-5286

BY FAX — To fax your order complete this order form and send to (+60-3) 282-1605

BY MAIL — Mail this completed order form to ***Periodica Islamica***
Berita Publishing

*SUBSCRIBERS IN MALAYSIA MAY PAY AN EQUIVALENT AMOUNT IN RINGGIT (M$) AT THE PREVAILING EXCHANGE RATE*

**Subscribe Now! Subscribe Now! Subscribe Now! Subscribe Now!**


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# COLUMBIA UNIVERSITY PRESS

*New...*

## ON SECURITY

Edited by
Ronnie D. Lipschutz
*240 pages / $17.50, paper / $49.50, cloth*
*New Directions in World Politics Series*
*Helen Milner and John Gerard Ruggie, General Editors*

The idea of global security has taken on new meaning in the post-Cold War world, compelling analysts of international relations to reassess the military, political, and cultural issues that intersect with the notion of security. ***On Security*** represents a wide range of views on shifting concepts of security at the turn of the millennium, when the tangible, bipolar arrangement of the Cold War-era world system no longer exists.

*New...*

## THE GENESIS OF CHINESE COMMUNIST FOREIGN POLICY

Michael Hunt
*336 pages / $34.50, cloth*

"An outstanding contribution to scholarship on modern Chinese history and modern international relations. It transcends existing 'fields' in the study of modern China with its easy mastery of the important literature of all of them and its bold use of newly available source materials."

—William Kirby, Harvard University

*New in paper...*

## THE ANARCHICAL SOCIETY

Hedley Bull
*335 pages / $17.50, paper*

"A masterful analysis of the problem of international order in contemporary society and of the feasibility of such alternative models as disarmament, global organization, a highly proliferated world, and a radical redistribution of wealth and power."

—*Foreign Affairs*

*New...*

## THE RWANDA CRISIS

History of a Genocide
Gérard Prunier
*250 pages / $29.95, cloth*

"In this first English-language analysis of the Rwandan genocide, Prunier speaks from the unique perspective of a knowledgeable but critical insider who is familiar with both the French establishment and the Rwandan Patriotic Front. In a lively and engaging voice, he offers the reader information unlikely to be found elsewhere."

—Alison Des Forges, Consultant, Human Rights Watch / Africa

*New...*

## ARMING JAPAN

Defense Production, Alliance Politics, and the Post-War Search for Autonomy
Michael Green
*250 pages / $40.00, cloth*

"The tension between Japan's urge for independence and its need for alliance with the U.S. has grown more relevant with the end of the Cold War. In my opinion no one covers this issue more cogently and readably than Michael Green."

—Thomas L. McNaugher, Brookings Institution

*New in paper...*

## THINKING THEORETICALLY ABOUT SOVIET NATIONALITIES

History and Comparison in the Study of the USSR
Edited by Alexander J. Motyl
*284 pages / $16.50, paper*

"An innovative and productive effort to bridge the chasm that has too long separated empirical studies of the Soviet nationality issues from theoretical work in contemporary politics."

—Joseph Rothschild, Research Institute on International Change

*New...*

## THE HINDU NATIONALIST MOVEMENT IN INDIA, 1925-1993

Christophe Jaffrelot
*360 pages / $32.50, cloth*

"Painstakingly researched and gracefully written."

—Amrita Basu, Amherst College

"This is the most systematic study I have seen on the topic of Hindu nationalism, a movement that has grown rapidly over the past decade and now poses a challenge to India's secular government . . . For the expert on South Asia, this book is an absolute must."

—Walter Andersen, *The Brotherhood in Saffron: A Study of Hindu Revivalism*

BUILDING ON 100 YEARS OF EXCELLENCE
COLUMBIA UNIVERSITY PRESS
FOUNDED 1893

At better bookstores.
Credit cards accepted.
Dept. 517, 136 South Broadway,
Irvington, NY 10533
Tel: (800) 944-8648
Fax: (800) 944-1844
Call or write for
our Political Science Catalog.
http://www.cc.columbia.edu/cu/cup


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

## GERMANY UNIFIED AND EUROPE TRANSFORMED

A Study in Statecraft

**Philip Zelikow and Condoleezza Rice**

*Bush Presidential Materials Project*

"For the first time, the inside story—what the policy-makers thought and did behind the scenes—is recounted by two participants, using interviews and secret documents...[The book] conveys the sweeping changes devised by a handful of leaders and their aides as they sought to capitalize on a rare, momentary acceleration of history."

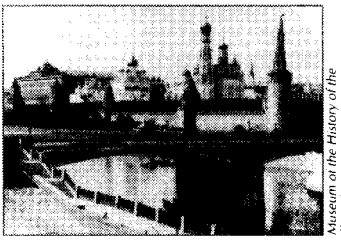
—Joseph Fitchett, *International Herald Tribune*

23 halftones $35.00 cloth

## MOSCOW

Governing the Socialist Metropolis

**Timothy J. Colton**



*Museum of the History of the City of Moscow*

"Colton's monumental history of twentieth-century Moscow promises to become the authoritative account of a pivotal period in the life of one of the world's great cities...An important contribution."

—Blair Ruble, Woodrow Wilson Center, Kennan Institute for Advanced Russian Studies, Washington, D.C.

Belknap Press January
64 halftones, 11 line illus., 43 tables, 41 maps
$45.00 cloth

## THE REBIRTH OF RUSSIAN DEMOCRACY

An Interpretation of Political Culture

**Nicolai N. Petro**

Nicolai Petro traces the long history of democratic aspirations in the Russian people, recovering for us an understanding crucial to our formation of successful foreign policy toward Russia.

1 line illus. $39.95 cloth

## POPULAR CONTENTION IN GREAT BRITAIN, 1758–1834

**Charles Tilly**

*© British Museum*

"A masterly study of changing forms of popular political action set within overarching arguments about the changing nature of the British state and polity."

—Lynn Hollen Lees, University of Pennsylvania

18 halftones, 22 line illus., 42 tables $49.95 cloth

## TRADING UP

Consumer and Environmental Regulation in a Global Economy

**David Vogel**

In this pioneering work, David Vogel analyzes the regulatory dimensions of all major international and regional trade agreements to challenge the conventional wisdom that trade liberalization invariably undermines national health, safety, and environmental standards.

$35.00 cloth

At bookstores or from

**Harvard University Press**

800-448-2242

http://www.hup.harvard.edu

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# PENN STATE PRESS

## On Humane Governance

*Toward a New Global Politics*

RICHARD FALK

In this volume commissioned by the World Order Models Project (WOMP), Falk provides a visionary account of the potential for global governance in the new world order based on nonviolence, respect for human rights, democracy, respect for international law, environmental balance, and planetary unity.

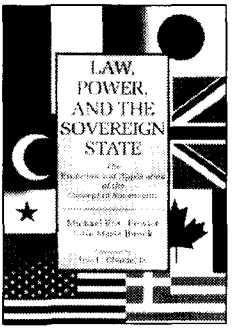
304 pages cloth: $45.00 paper: $16.95

*For sale in the U.S. and Canada only*

## Law, Power, and the Sovereign State

*The Evolution and Application of the Concept of Sovereignty*

MICHAEL ROSS FOWLER AND JULIE MARIE BUNCK




"This invaluable study of sovereignty explores anew one of the most enduring ideas in political theory and illuminates with lucidity the changing nature of the sovereign state."
—Richard Falk, Princeton University

214 pages cloth: $28.50 paper: $13.95

*Available in bookstores or from*

**PENN STATE PRESS**
820 N. University Drive
University Park, PA 16802
Orders: **1-800-326-9180**

## Greece at the Crossroads

*The Civil War and Its Legacy*

EDITED BY JOHN O. IATRIDES AND LINDA WRIGLEY

A collection of essays by European, American, and Australian specialists offering new and authoritative analyses of the Greek civil war and its international dimension.

352 pages cloth: $55.00 paper: $18.95

## The Caribbean Legion

*Patriots, Politicians, Soldiers of Fortune, 1946–1950*

CHARLES D. AMERINGER

A tale of adventure and intrigue, *The Caribbean Legion* studies the political struggles of the peoples of Costa Rica, Cuba, the Dominican Republic, Guatemala, Honduras, and Nicaragua in the years following World War II.

184 pages cloth: $35.00 paper: $15.95

## From the Polish Underground

*Selections from* Krytyka, *1978–1993*

EDITED BY MICHAEL BERNHARD AND HENRYK SZLAJFER

"Much needed and highly welcome. It will provide an indispensable source for virtually anybody who, as a scholar, political analyst, journalist, teacher, student, or just general reader, wishes to gain insight into the extremely complex matter of the emerging new political thought in the countries of the former East Bloc." —Stanislaw Baranczak, Harvard University

486 pages cloth: $75.00 paper: $19.95


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# Examining the World

## WILD LILY, PRAIRIE FIRE

China's Road to Democracy, Yan'an to Tian'anmen, 1942–1989

**EDITED BY GREGOR BENTON AND ALAN HUNTER**

Gregor Benton and Alan Hunter provide here a source book of documents of democratic dissent under Chinese Communism, most of them previously untranslated and difficult to find in the West. Ranging from eye-witness accounts of a massacre to theoretical critiques of Chinese Marxist thought, these essays are among the most powerful and important works of Chinese dissident literature written in this century. The story of Chinese Communism has often been reduced to uniformity not only by political bureaucrats in China but by Western scholarship derived from official Chinese histories. *Wild Lily, Prairie Fire* paints a far richer picture.

**"[A] valuable source book. . . . Highly recommended."**—*Library Journal*

Paper: $19.95 ISBN 0-691-04358-2 Cloth: $49.50 ISBN 0-691-04359-0

## SATELLITES AND COMMISSARS

Strategy and Conflict in the Politics of Soviet-Bloc Trade

**RANDALL W. STONE**

Why did the Soviet Union squander the political leverage afforded by its trade subsidy to Eastern Europe? Why did Soviet officials fail to bargain with resolve, to link subsidies to salient political issues, to make credible commitments, and to monitor the satellites' policies? Using an unprecedented array of formerly secret documents housed in archives in Moscow, Warsaw, and Prague, as well as interviews with former Communist officials across Eastern Europe, Randall Stone answers these questions and others that have long vexed Western political scientists.

Stone draws upon recent developments in bargaining and principal-agent theory, arguing that the incentives created by domestic institutions weakened Soviet bargaining strategies. In effect, he suggests, perverse incentive structures in the Soviet economy were exported into Soviet foreign policy. Furthermore, Stone argues, incentives to smother information were so deeply entrenched that they frustrated numerous attempts to reform Soviet institutions.

**"A very useful contribution to the field, drawing upon a wide range of interviews and newly available documents. It is very interesting and well written, and it casts new light on Eastern European and Soviet politics."**
—Alec Nove, University of Glasgow

*Princeton Studies in International History and Politics*
*John Lewis Gaddis, Jack L. Snyder, and Richard H. Ullman, Editors*

Cloth: $35.00 ISBN 0-691-04414-7 *Available February 1996*

LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# CURRENCY AND COERCION

The Political Economy of International Monetary Power

**JONATHAN KIRSHNER**

Jonathan Kirshner here examines how states can—and have—used international currency relationships and arrangements as instruments of coercive power for the advancement of state security. Kirshner succeeds in developing a generalized framework for the analysis of an important yet neglected form of state power that is likely to be of increasing importance in the post-Cold War era. Although some distinguished scholars have touched on the issue of monetary power, there has been until now no standard text on the subject.

Cloth: $39.50 ISBN 0-691-03768-X

# DOES CONQUEST PAY?

The Exploitation of Occupied Industrial Societies

**PETER LIBERMAN**

Can foreign invaders successfully exploit industrial economies? *Does Conquest Pay?* demonstrates that expansion can, in fact, provide rewards to aggressor nations. Peter Liberman argues that invaders can exploit industrial societies for short periods of time and can maintain control and economic performance over the long term. This is because modern societies are uniquely vulnerable to coercion and repression. Liberman's work suggests that the international system is more war-prone than many optimists claim.

*Princeton Studies in International History and Politics:*
*John Lewis Gaddis, Jack L. Snyder, and Richard H. Ullman, Editors*

Cloth: $35.00 ISBN 0-691-02986-5 *Available January 1996*

# FROM THE OUTSIDE IN

World War II and the American State

**BARTHOLOMEW H. SPARROW**

*From the Outside In* examines the profound impact of World War II on American government. The book argues that the wartime and immediate postwar experiences of the 1940s transformed and redirected the policies and government institutions of the New Deal. In it, Bartholomew Sparrow proposes a new model of the state and of "state-building."

The book will lead readers to reevaluate the impact of international factors on American political development, to reappraise the role of the New Deal in shaping the postwar federal government, and to reconsider the application of organizational theory to American government.

*Princeton Studies in American Politics: Ira Katznelson, Martin Shefter, and Theda Skocpol, Editors*

Cloth: $39.50 ISBN 0-691-04404-X *Available February 1996*

# PRINCETON UNIVERSITY PRESS

AVAILABLE AT FINE BOOKSTORES OR DIRECTLY FROM THE PUBLISHER: 800-777-4726
WORLD WIDE WEB SITE: HTTP://AAUP.PUPRESS.PRINCETON.EDU/PUPRESS


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# Security Dialogue

Edited by **Magne Barth** *International Peace Research Institute, Oslo (PRIO)*

"A beacon of world intellect and conscience for world peace."
**Dr. Kim Dae-jung, Chairman, KPF**

**Security Dialogue** serves as a channel of communication between researchers, international civil servants, journalists, politicians, NGOs, diplomats and the military. The journal seeks to provoke reflection through interregional dialogue on issues of global security along a variety of dimensions: the new international system, politics of fusion and fragmentation of states, as well as military, economic, political and environmental aspects.

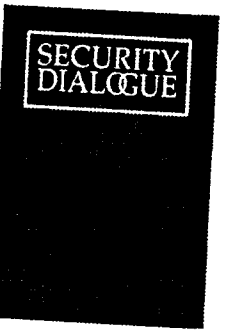
**Your 1995 subscription includes:**

- **Ingvar Carlsson** Roles for the UN in International Security After the Cold War
- **Christoph Bertram** NATO on Track for the 21st Century
- **Robert J. Mathews and Timothy L. H. McCormack** Entry into Force of the Chemical Weapons Convention
- **Kim Hakjoon** On North Korea After Kim Il-sung
- **Janusz Stefanowicz** Central Europe Between Germany and Russia
- **Alexei Arbatov** NATO and Russia
- **Max Ahmadau Sesay** Collective Security or Collective Disaster? Regional Peacekeeping in West Africa
- **Hans-Peter Gasser** The Geneva Conventions and the Autonomous Territories in the Middle East
- **Gheorghe Tinca** Securing a Democratic Romania: No Veto on our Choice
- **Daisaqu Ikeda** Creating a Century without War through Human Solidarity
- **Aabha Dixit** India-Pakistan: Are Commonly Accepted Confidence Building Structures Relevant?
- **Documentation:** NPT Review and Extension Conference, 17th April-12th May 1995

**(ISSN: 0967-0106)**
**Published quarterly in March, June, September and December**

Don't forget, we guarantee that if you are dissatisfied with your journal in any way, we will refund the cost of your subscription.

## *Subscribe at the introductory rate*




## *Order Form for New Subscribers*

**SAGE Publications Ltd**
**6 Bonhill Street, London EC2A 4PU, UK**
Tel +44 (0)171 374 0645
Fax +44 (0)171 374 8741

USA orders to be sent to:
**PO Box 5096, Thousand Oaks, CA 91359**

☐ Yes! I want to subscribe to *Security Dialogue* starting with Volume 26 (1995) at the:

☐ **Introductory Rate for New Subscribers** £24 /$38 (usual rate £30/$48)

☐ **Institutional Rate** £89/$142

## *Methods of Payment*

☐ **CHEQUE...** I enclose a cheque (made payable to **SAGE Publications Ltd**) for: ☐

☐ **CREDIT CARD...**
Please invoice my credit card

☐ Mastercard ☐ Access ☐ Eurocard
☐ Diner's Club ☐ American Express ☐ Visa

Amount ☐

Card No: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

Expiry Date: ☐/☐

Signature: _____ Date: / / .

Name _____

Address _____

_____

_____ 5857


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED

# Examining the World

## ISOLATIONISM RECONFIGURED

American Foreign Policy for a New Century

**ERIC A. NORDLINGER**

This iconoclastic and fundamental work, Eric Nordlinger's last, advocates a new variant of isolationism, a "national strategy" confining U.S. military actions largely to North America and to neighboring sea- and air-lanes but encouraging international activism and engagement in nonsecurity realms. In Nordlinger's view, disengaging from security commitments on distant shores would liberate the United States to use its resources and decision-making powers to act more effectively abroad in matters of economic policy and human rights. A national strategy would then become a powerful new method of encouraging international ideals of democracy, and isolationism would be freed of its previous associations with appeasement, weakness, economic protectionism, and self-serving nationalism.

**"One of the most original, provocative and important foreign policy books to appear in years."**—Samuel P. Huntington, Harvard University

Cloth: $29.95 ISBN 0-691-04327-2

## COOPERATION AMONG DEMOCRACIES

The European Influence on U.S. Foreign Policy

**THOMAS RISSE-KAPPEN**

In exploring the special nature of alliances among democracies, Thomas Risse-Kappen argues that the West European and Canadian allies exerted greater influence on American foreign policy during the Cold War than most analysts assume. In so doing, he challenges traditional alliance theories that emphasize strategic interactions and power-based bargaining processes.

Through detailed case studies, Risse-Kappen shows that the Europeans affected security decisions concerning vital U.S. interests during the 1950–1953 Korean war, the 1958–1963 test ban negotiations, and the 1962 Cuban missile crisis—all during a span of time in which the U.S. enjoyed undisputed economic and military supremacy in the alliance. He then situates these case studies within a theoretical framework.

The book's findings have important repercussions for the post-Cold War era in that they suggest the transatlantic security community is likely to survive the end of the Soviet threat.

**"The aims of this book are ambitious, and Thomas Risse-Kappen succeeds in fulfilling them. . . . A serious contribution to theory on cooperation among democracies."**—Bruce M. Russett

*Princeton Studies in International History and Politics: John Lewis Gaddis, Jack L. Snyder, and Richard H. Ullman, Editors*

Cloth: $35.00 ISBN 0-691-03644-6

## PRINCETON UNIVERSITY PRESS

AVAILABLE AT FINE BOOKSTORES OR DIRECTLY FROM THE PUBLISHER: 800-777-4726
WORLD WIDE WEB SITE: HTTP: //AAUP.PUPRESS.PRINCETON.EDU/PUPRESS


LICENSED TO UNZ.ORG
ELECTRONIC REPRODUCTION PROHIBITED